STATE OF LOUISIANA
DIVISION OF ADMINISTRATION
OFFICE OF COMMUNITY DEVELOPMENT

WORKSHOP MANUAL

for Recipients of the

LOUISIANA COMMUNITY DEVELOPMENT BLOCK GRANT

TABLE OF CONTENTS

Section I. Introduction

The Office of Community Development (OCD) is a primary recipient of Community Development Block Grant funds from the U.S. Department of Housing and Urban Development, and administers nonentitlement grants to local governments in the State of Louisiana (the LCDBG program).

As a primary recipient, the Office of Community Development is responsible to see that local governments (subrecipients) who receive Block Grant funds through the OCD have met all of the requirements applicable to the use of such funds. Under the provisions of Office of Management and Budget (OMB) circular A-133, this means that the OCD must:

1. Determine whether the local government has met the audit requirements of Circular A-133;

2. Determine whether the subrecipient spent federal assistance provided in accordance with applicable laws and regulations;

3. Ensure that appropriate corrective action is taken within six months after receipt of the subrecipient audit report for any reported instances of noncompliance;

4. Consider any adjustments that may be necessary, based on the results of the subrecipients' audits, and

5. Require each subrecipient to permit independent auditors to have access to their records and financial statements as necessary to comply with Circular A-133.

In order to meet its responsibilities, OCD has developed and furnished to each subrecipient a copy of the 1997 Community Development Block Grant Program Grantee Handbook ("the Handbook") . The Handbook sets forth all of the applicable requirements for Program Administration, Public Facility Improvements programs, Housing Rehabilitation programs, Real Property Acquisition, Relocation/Demolition, Economic Development programs, Antidisplacement, as well as Monitoring and Closeout provisions.

This manual is aimed at extracting the financial management and administrative requirements for explanation purposes, promoting a better understanding of those requirements, and serving as a reference source to administrators and financial managers responsible for day-to-day operations of the Block Grant program.

This material will explain the applicable principles of fund accounting necessary to record transactions occurring in the program, the accounting procedures to be followed, laws and regulations applicable to the program and suggested administrative controls, the audit requirements, the monitoring process, and will offer a comprehensive case study to illustrate the principles and techniques included in the text.

Subrecipients are requested to use this manual whenever a question regarding the program occurs in an attempt to find a solution to the problem, as every attempt has been made to include every possible type of transaction that could occur. If a satisfactory answer cannot be found, subrecipients should then contact the OCD for technical assistance in resolving the matter. For convenience, a contact list of persons at the OCD has been included in the appendix, to assist the subrecipient in directing inquiries to the appropriate OCD personnel.

Section II. Principles of fund accounting

Principles applicable to governmental accounting are established by the Governmental Accounting Standards Board (GASB), and are included in the Codification of Governmental Accounting and Financial Reporting Standards (the *Codification*). That publication states that "Financial reporting is not an end in itself, but is intended to provide information useful for many purposes. Financial accounting helps fulfill government's duty to be publicly accountable."

Proposed changes by the GASB

The GASB has proposed dramatic changes to the governmental reporting model which will require additional reporting of state and local governments' activities at the entity wide level, inclusion of management's discussion and analysis, in addition to traditional fund perspective financial statements. The entity wide perspective financial statements will separate governmental activities from business-type activities, include all fixed assets and long-term debt in the balance sheet, require the recording of depreciation on general fixed assets, including infrastructure (roads, bridges, etc.), and activities will be presented on the accrual basis of accounting, using the economic resource measurement focus. In essence, governmental financial statements, at least at the entity wide perspective, will look much more like the financial statements of businesses.

By far, the most unpopular requirement of the proposed change is the mandatory capitalization of infrastructure. The intention is that beginning at the effective date, all new infrastructure must be capitalized, and governments would be allowed three years to accomplish recordation of "major infrastructure assets" at their historical or estimated historical cost, including recognition of accumulated depreciation. This will require a substantial amount of research, inventorying of existing infrastructure, and establishing some plan to determine the actual cost or estimated cost of the assets, as well as calculating the depreciation accumulated at the date of adoption.

Management of state and local governments will be required to include a discussion and analysis, which places the governmental unit's financial position and results of operations in narrative form. This discussion will consider both positive and negative transactions and events, and the use of charts and graphs to illustrate activities and trends is recommended (but not required).

The fund perspective retains the use of modified accrual accounting for governmental activities. The account groups (fixed assets and long-term debt) are no longer presented at the fund perspective.

Users of this manual should be alert to the status of this proposal. GASB plans to adopt the proposal in mid-1998, with the planned effective date in the year 2000. The existing infrastructure would be required to be included in assets by the year 2003. Upon adoption, the principles presented in this manual will be superseded, and users will be required to follow the applicable generally accepted accounting principles (GAAP) as established by GASB. The remainder of this section is based on GAAP existing as of the date of this writing (1997).

Existing GAAP

Financial reporting by governmental entities has two purposes. The first is to fairly present financial position and results of operations in accordance with the prescribed accounting principles. The second, no less important than the first, is to demonstrate compliance with applicable laws and regulations (*Codification* Sec. 1200).

Compliance is a matter of paramount importance in the governmental accounting process, due to the highly regulated nature of governmental operations. Laws and regulations are prescribed to control governmental operations due to the responsibility to the taxpaying public. We refer to that responsibility as ***accountability***.

Accountability is owed to the taxpayers based on the fact that government takes its authority from the taxpayers. The individuals who constitute a government, whether it be a village, town, city, parish, state or nation, give to the government (among other rights) the power to tax involuntarily. Accordingly, how those taxes are administered is closely controlled by laws and regulations, which are reflective of the taxpayers' concerns and needs.

Control Mechanisms

The *Codification* provides that certain control mechanisms have evolved to ensure that resources provided to a government are used as intended. One such mechanism is the **budget**.

Budgets are believed to be the most significant financial document produced by a governmental entity. It is a plan for coordination of revenues and expenditures for a particular purpose. Virtually every government in the State has an annual operating budget requirement for certain activities. Although not required by law, some governments also prepare long-term budgets for capital improvements, which is recommended for Block Grant activities, whether accounted for in capital projects or special revenue funds. Both the fund types and budgetary requirements will be discussed in detail later in the text. Capital budgets are plans for proposed capital outlays and the means of financing them for periods which may exceed one year.

Another control mechanism which has evolved is ***fund accounting***. The financial and legal requirements and restrictions leading to fund accounting need to be considered as part of the government's duty to be accountable. The *Codification* provides that governmental accounting systems should be organized and operated on a fund basis.

A **fund** is defined as a "fiscal and accounting entity with a self-balancing set of accounts recording cash and other financial resources, together with all related liabilities and residual equities or balances, and changes therein, which are segregated for the purpose of carrying on specific activities or attaining certain objectives in accordance with special regulation, restrictions, or limitations." (*Codification* Sec. 1100.102).

The *Codification* identifies three broad fund categories (governmental, proprietary and fiduciary funds) and within those categories seven fund types (general, special revenue, capital projects, debt service, enterprise, internal service, and trust/agency funds).

Governmental funds are those through which most governmental functions are typically financed. They represent accounting segregations of financial resources. That is, governmental funds account for expendable assets according to the purpose for which they must be used, the current liabilities to be paid from those assets, and any difference between those assets and liabilities is presented as "fund balance".

Careful consideration has been given to the various fund types presented in the *Codification* in determining the appropriate fund type to account for activities under the LCDBG program. The fund type deemed to be most appropriate for construction type grants is the *capital projects fund*. Alternatively, governments may use *special revenue funds* to account for nonconstruction type programs (such as street reconstruction or overlay programs). Recipients should be aware that different budget requirements apply to each of these fund types. **Regardless of the fund type used, OCD requires that a separate fund be established to account for the LCDBG activities**. **The separate fund should account for all LCDBG activities, including any state or local matching funds which are expended on the program.**

Capital Projects Funds

Capital projects funds are used to account for financial resources to be used for the acquisition or construction of major capital facilities (other than those financed by proprietary or trust funds) (*Codification* Sec. 1300.103a(3)).

The capital projects fund was selected because most frequently, LCDBG grants finance the construction of capital facilities such as water treatment, sewer treatment, improvements to such existing facilities, or other capital assets, such as fire protection. It is insignificant that other incidental activities may also be included. Likewise it is insignificant that the facilities constructed may be used in, for example, an enterprise activity, such as a water or sewer enterprise fund.

Another reason that the capital projects fund was selected is that an annual operating budget is not required under either the accounting principles in the *Codification* or under the Local Government Budget Act (La. R.S. 39:1301 et seq.). This allows the use of a capital budget or *project budget*, rather than an annual budget. Since activities conducted in the LCDBG program frequently are carried out in more than one fiscal year, a project budget is more helpful than an annual operating budget in controlling expenditures applicable to the program.

If the project provides for construction of enterprise fund assets (water and sewer improvements, for example), the accumulated capital expenditures are recorded (normally at year end) in the enterprise fund as construction in progress (debit) and contributed capital (credit). Upon completion of the project, the construction in progress balance is transferred to the appropriate fixed asset account, and when placed in service, depreciation is recorded on those assets.

Special Revenue Funds

Special revenue funds are used to account for the proceeds of specific revenue sources (such as LCDBG) that are legally restricted to expenditures for specified purposes (*Codification* Sec. 1300.103a(2)).

As stated above, recipients may elect to use the special revenue fund to account for LCDBG activities, particularly those which do not finance construction of fixed assets. The use of the special revenue fund to account for grant activities does require the adoption of an annual operating budget under the Local Government Budget Act (La. R.S. 39:1301 et seq.) The grant budget must therefore be adopted in the government's regular budget process, and is subject to the same requirements (such as publication and amendments) as the otherwise adopted budget. Recipients should also be aware that accounting for the grant activities in the special revenue fund may cause small entities to become subject to public hearing requirements that would otherwise not apply.

Basis of Accounting

The *Codification* provides that governmental fund (including capital projects fund) revenues and expenditures should be recognized on the *modified accrual* basis of accounting. The term "basis of accounting" refers to ***when*** assets, liabilities, revenues and expenditures should be recognized in the accounts and reported in the financial statements. Specifically, it relates to the timing of the measurements made.

So what is the "modified accrual" basis of accounting? How does it differ from other bases of accounting, such as the "accrual basis" or the "cash basis"?

First, consider the cash basis of accounting, since many local governments in Louisiana maintain their records on the cash basis. Under the cash basis, revenues are not recorded until the cash is received, and expenditures are not recorded until cash is disbursed. For those units of government following the cash basis, this means that the transactions that are recorded in the accounts are simply bank deposits and checks. If the bank account is reconciled to the general ledger at the end of each month, this provides some assurance that all transactions are recorded, and that they are recorded at the proper dollar amount.

The accrual basis, on the other hand, records transactions when the underlying *event* takes place, rather than when the cash is received or expended. "Event" may refer to several things. On the revenue side, one such event is the levy of property taxes (as opposed to the *collection* of such taxes). Likewise, the "event" for sales tax recognition is the actual sale giving rise to the tax, as opposed to the actual collection of the tax.

On the expenditure side, the acceptance of goods or services is an "event" that would constitute an expenditure under the accrual basis, even though the government may not actually pay for the goods or services until a later time.

The accrual basis is appropriate for some activities of local governments. For example, activities of a water enterprise fund should be recorded on the accrual basis. It is appropriate, in that context, to record revenue when the water customer uses the water, normally billed at the end of each month, rather than when the water customer actually pays his or her bill for the service. The government should record revenue as it is billed (a credit to revenue), and a corresponding increase (a debit) in *accounts receivable* to reflect the fact that amounts owed to the government have increased as a result of the customer's water use. The subsequent collection of the cash in settlement of the amount due merely increases cash and reduces the accounts receivable (the amount owed). The revenue has already been recorded when the service was billed to the customer.

The accrual basis is considered superior to the cash basis, since it provides a better measure of the economic realities. It reflects the actual substance of the transactions, rather than merely when cash is received or disbursed.

Unfortunately, the terms "accrual" and "accrual accounting" are often interpreted to mean "income determination accounting", and thus connote the measurement of *expenses* (including depreciation expense), which are not related to governmental fund activities. Governmental funds (such as capital projects and special revenue funds) do not record expenses; they record *expenditures,* which differ somewhat from expenses. *Expenses* are <u>always</u> recognized when the related liability is incurred, and include the using up of economic assets ("depreciation" expense, as discussed below); expenditures are <u>generally</u> recognized when the related liability is incurred, and <u>never</u> include depreciation. Hence, the term "modified accrual" basis was coined to make the distinction.

<u>Modified Accrual Basis of Accounting</u>

The major differences in applying the accrual concept in governmental fund accounting (as opposed to proprietary funds or commercial enterprises) relate to differences in the environment and the accounting measurement objectives.

Proprietary funds (such as water and sewer enterprise funds) and commercial businesses are concerned with their *net income*. Their operating statements reflect revenues and expenses, including depreciation expense. Depreciation is a reflection of the "using up" of economic resources, such as buildings, furniture and fixtures, and equipment.

Governmental fund activities, however, are not concerned with the using up of such assets. Their activities measure only *current financial resources,* rather than *current or noncurrent economic resources*.

Accordingly, the measurement focus for governmental fund activities is different from commercial activities, either in proprietary funds or in commercial businesses. Some distinction are therefore required in both terminology and how transactions are measured.

Finally, then, we consider the *modified accrual* basis of accounting, which is applicable to either the capital projects or special revenue funds we have declared as appropriate to the LCDBG program.

Revenues are recognized under the modified accrual basis in the period in which they become (both) *measurable* and *available*. "Measurable" simply means that the dollar amount is determinable. "Available" means collectible within the current accounting period or soon enough thereafter to be used to pay liabilities of the current accounting period.

What is "soon enough thereafter"? That depends upon how the government defines the term; however, the time period should not exceed sixty days, normally. In other words, if the amounts will be collected within sixty days after the end of the current accounting period, it is appropriate to recognize the revenue in the current accounting period.

Under the modified accrual basis, expenditures (decreases in net financial resources) are generally measurable, and should be recorded when the related liability is incurred.

What does all this mean in the context of the LCDBG program? We will explore this in substantial detail in the comprehensive example following the text, but a simple explanation is as follows. Whenever goods or services are provided to the government in connection with the LCDBG program, it is appropriate to recognize an expenditure and the related liability (accounts payable) at the time the amount is determinable. Normally, that is when the amount is invoiced to the program.

The LCDBG program is operated on a reimbursement basis. This is typically referred to as an *expenditure driven* program. That means that when the expenditures are incurred in accordance with the program requirements, in addition to recording that expenditure, it is then appropriate to record the revenue and related asset (an account receivable), since the grant revenue is then due to the local government.

Example Assume that an LCDBG recipient has received its first invoice for services rendered to the program from its consultant for $5,000. The result of the preceding discussion is that when the invoice is received, the government will record:

1. The expenditure:

Administrative expenditures	5,000.00	
Accounts payable		5,000.00

<u>and</u>

2. The revenue:

Grant revenue receivable	5,000.00	
LCDBG revenue		5,000.00

Under normal circumstances, the expenditure and the revenue will be recorded at approximately the same time, in equal amounts, as all the necessary criteria have been met at the time of invoicing by the vendor, in this case, the consultant. As a practical matter, the revenue entry is normally recorded when the Request for Payment is prepared.

In general, Requests for Payment are prepared after an expenditure has been *incurred* but not paid, in which case the actual check will be written immediately after the program funds are received (within three days), and will be made payable to the vendor. In the example above, the entry to record the check in this instance will be as follows:

Accounts payable	5,000.00	
LCDBG program cash		5,000.00

Assume however, that the general fund pays the consultant immediately upon receipt of the invoice. The entry to record the expenditure in the general fund is as follows:

Due from LCDBG fund	5,000.00	
General fund cash		5,000.00

The LCDBG program fund then records the following entries:

1.	Administrative expenditures	5,000.00	
	Due to general fund		5,000.00
2.	Grant revenue receivable	5,000.00	
	LCDBG revenue		5,000.00

When the Request for Payment is received, the entry to record the disbursement in the LCDBG program is as follows (the check is made payable to the general fund):

Due to general fund	5,000.00	
LCDBG program cash		5,000.00

The general fund entry to record the reimbursement is:

General fund cash	5,000.00	

Due from LCDBG fund 5,000.00

By way of comparison, the *cash basis of accounting* would not record anything until the cash was actually received and checks written and released. The revenue entry (credit) would be offset by a debit to cash, and the expenditure entry (debit) would be offset by a credit to cash.

The objective of the modified accrual basis, then, is simply to recognize the revenues and expenditures before they become cash transactions. At the completion of the program (when all activities are finished and the program is "closed out"), there will be no differences between the cash and modified accrual bases of accounting for the transactions. Use of the modified accrual is simply a matter of timing.

Standard Chart of Accounts

To accomplish the recording of transactions in a consistent and complete manner, the OCD has developed a standard chart of accounts (Exhibit A-25 in the 1997 Handbook). It is reproduced on page 27 for reference.

The focal points of the standard chart of accounts at this point are the following:

Account name	Number*	Purpose of Account
Grant revenue receivable	13	To record amounts due to the local government from the OCD but not yet collected
Accounts payable	51	To record amounts due to vendors and suppliers which are not yet paid
Contracts payable	52	To record amounts due to contractors which are not yet paid
Expenditures	81-84	To record expenditures incurred for goods and services (administration, acquisition, engineering, construction, etc.)
Revenues	91-94	To record revenues (LCDBG program, program income, local matching, or any other funds to be used in project, such as FmHA) when measurable and available

* For illustration only

For individual projects, accounts may be added to reflect the line items included in the approved grant document, such as "Code Enforcement" or "Clearance and Demolition" in the expenditures portion of the chart. A numbering sequence similar to that shown above is suggested.

In order to apply the modified accrual basis of accounting to the LCDBG program, the following matters are of significance:

- When an invoice is received for goods or services, an expenditure is incurred. At that point, the modified accrual basis requires a debit to the appropriate expenditure account (accounts 81 through 84), with a corresponding credit to either accounts payable (account 51) or contracts payable (account 52), as appropriate.

- At the time expenditures are recorded it is also appropriate to record the corresponding revenue, since revenue recognition is “expenditure driven”, and both the *measurable and available* criteria are met. The entry is to debit grant receivable (account 13) and the corresponding credit is to LCDBG revenue (account 91), for the same amount recorded as the expenditure.

- In some situations, there are neither program income nor local matching funds, so that the assets and liabilities are equal (and as a result there is no net difference or "fund balance"). Likewise, the revenues and expenditures would be equal. In those situations, then, any differences between assets and liabilities or between revenues and expenditures should be investigated to determine whether all amounts have been recorded as both asset and corresponding revenue and liability and corresponding expenditure.

- In other programs, there are other funds involved, such as from FmHA. In such programs, assets and liabilities will typically not be equal.

- Following the transactions to their completion, when the reimbursement is received from the OCD, the entry to record the receipt is a debit to cash (account 01) and a credit to grant revenue receivable (account 13). When the checks are prepared and released, the entry to record them is a debit to accounts or contracts payable (accounts 51 or 52, as appropriate) and a credit to cash (account 01).

Section III. <u>Accounting procedures</u>

<u>Basic Documentation Requirements</u>

A commonly asked question among local governments is "What records am I required to maintain?", and secondarily, "How long should I keep them?". The basic supporting documentation for expenditures under the LCDBG program is no different than that required for other expenditures, although additional laws and regulations apply to program expenditures. For purposes of the LCDBG program, “adequate documentation” is defined as follows:

- **Purchase orders** Purchase orders provide a basic minimum control over expenditures of a governmental unit. Purchase orders should be prenumbered, and periodically the sequence of used purchase orders should be accounted for. Should any items be discovered as missing, appropriate follow up would include determining the status of those purchase orders not accounted for, and posting missing item numbers in a place where they may be referred to so that those numbers may not be used to justify any current or future purchases. Blank purchase orders should be kept under strict control to prevent unauthorized use. Voided purchase orders should be defaced (boldly marked "VOID") and retained to satisfy the accounting sequence test described above. Properly completed purchase orders should include the vendor name, date the purchase was authorized, the item description (clearly explained) including item number, if applicable, and the price of the item, if known. It is also beneficial to indicate the use of the item, for example, indicate whether the item is to result in an expenditure of the general fund, LCDBG program, or some other activity or department. **Purchase orders should be signed by a responsible official in accordance with the entity's policies**.

  Duplicate forms are recommended. This allows the original to be mailed or taken to the vendor, and the duplicate may be retained for filing with the invoice upon payment. Open purchase orders should be filed separately pending receipt of the original vendor invoice. Periodically, the open purchase order file should be reviewed for unmatched orders substantially out of date. Such items should be investigated, and compared to unmatched vendor invoices.

- **Original vendor invoices** An original vendor invoice is essential prior to any action towards payment of an amount for either goods or services. **Copies should <u>never</u> be used to justify payments, and when payment is made, the original vendor invoice should be defaced (boldly marked "PAID" along with the check number and date paid) to prevent duplicate payment**. Prior to payment approval, **a responsible official should have determined** that the goods or services were actually received, in the quantities billed, and compared the invoice to the approved purchase order to determine that the purchase was approved prior to invoicing. **Such review and determination should be evidenced by the**

individual's initials and the date that the determination was made. Some governments employ **receiving reports** to accomplish documentation of this review.

Any invoices not bearing the purchase order number or invoiced prior to the purchase order date should be investigated fully before payment, and discrepancies should be addressed to the appropriate parties to prevent recurrence.

- **Checks and other bank records** OCD requires that a separate checking account be established for each grant, in order that **all** checks be accounted for upon monitoring. In addition, preprinted, prenumbered checks are to be used, and unused checks should be secured by the grantee. Two part checks are recommended, allowing the original to be mailed to the vendor, with the duplicate retained with the additional documentation (attached to the purchase order, invoice, etc.). This is required where the depository banks do not return canceled checks.

  Likewise, it is highly recommended that checks have two signatures to be valid. The use of signature stamps or signing plates is discouraged.

  If returned by the depository bank, canceled checks (and deposit slips) should be retained with the bank statement at month end, to facilitate reconciliation of the bank statement, as well as provide documentation of the bank statement amounts upon audit or review by supervisory personnel.

- **Deposit slips** Although grant funds received from the OCD are directly deposited into the grantee's account, other sources of funds may be received and deposited by the local government. In that case, deposit slips should be prepared in duplicate. Both copies should be presented to the teller for deposit, with the original maintained by the bank, and the duplicate returned to the person making the deposit, after validation by the teller. The duplicate serves as proof that the amount was actually deposited until the bank statement is received and the account reconciled.

  Deposit slips should contain sufficient information to enable a disinterested person to determine the source of the deposit, date the deposit was made, and the individual amounts that made up the deposit.

- **Bank reconciliations** Bank accounts should be reconciled immediately upon receipt of the bank statement. The reconciliation may be made on a separate schedule, on the form typically provided on the back of the statement, or if available, using computer software designed for that purpose.

  Reconciliations should be initialled and dated by the person performing the reconciliation, as well as any person performing a review of the reconciliation. Journal entries required to accomplish reconciliation of the account (such as to record check charges, etc.) should be prepared, reviewed and posted as soon as possible after reconciliation of the statement. Any discrepancies in checks or deposits should be reported to the depository bank as well as supervisory officials (the elected officials of the local government or OCD representatives) within ten days of receipt of the bank statement.

- **Payroll records, payroll tax returns, retirement system reports, Forms W-2** Payroll records are essential parts of personnel administration. Such records begin with the personnel file, which should include the application or other employment forms (resumes, transcripts, etc.), the W-4 and L-4 (federal and state withholding statements), I-9 (immigration and naturalization forms), employment history forms or other memoranda indicating the date hired, position, starting salary, and the person who made the decision to hire. Personnel change notices (wage or salary increases, promotions, transfers, terminations) should require proper signatures and be included in the personnel file documentation as well. In addition, any deductions from the employees' pay (for insurance, etc.) should be authorized by the employee in writing, and such approval included in the personnel file.

  Payroll tax returns, retirement system reports, W-2's and similar documents should be prepared as soon as possible and employer copies retained in a safe place for future reference.

  Payroll preparation requires that there be some record of the time worked, **even for salaried employees**. This is particularly true for payroll charges to federally funded programs, which include the LCDBG program. All amounts charged to the program must be adequately supported by vendor invoices (for goods and services) or time sheets, time cards, etc., (for payroll charges). Time records must be approved by the employees' immediate supervisor. Calculation of the gross payroll, may be performed by computer software or manually. If prepared manually, calculations should be recorded to indicate the hours worked and the salary or wage rate to arrive at gross pay. Deductions should be clearly indicated and authorized by law or the employee to determine the net pay. For employees who work on only one cost objective, no additional documentation is required.

  However, when an employee works on *multiple cost objectives*, additional documentation is required to support charges to the LCDBG grant. Salary distributions among the various cost objectives must be supported by personnel activity reports or time sheets (such as 1997 Handbook Exhibit A-30) which must:

  - reflect an actual after-the-fact distribution of the employees' activity

  - account for the total of the employees' activities

  - be prepared at least monthly and coincide with one or more pay periods

  - be signed by the employee

Budgeted estimates determined in advance do **not** qualify as supporting documentation. Estimates may only be used for interim purposes, and must be adjusted at least quarterly.

- **Retention requirements** State law requires that the above records be retained for a minimum of three years, or until audited, whichever is longer. Experience indicates that a longer period may be advisable, particularly with respect to the payroll records. A minimum of seven years is recommended for payroll records.

- **Certain records should never be destroyed**. These include the minutes of the governing body, laws and ordinances, and financial reports.

Basic Records to be Maintained

The type and extent of records maintained by local governments varies widely, according to the nature and activities of each individual government. Those who provide numerous services, and whose revenue sources are varied require more complex records than those providing only basic services from one or two revenue sources.

Some local governments keep records manually. Others utilize computerized systems, which may employ personal computers (PC's), minicomputers or mainframes.

Given these differences, basic records maintained are essentially the same, or at least produce the same basic information. Since it is not possible in this context to address every possibility, the procedures to be followed and records to be produced are hereafter illustrated in manual form, i.e., they way they might look if the records were maintained by hand as opposed to computer-based systems.

The basic books of record for all entities are the cash receipts journal, cash disbursements journal and general ledger, with necessary adjustments recorded in and posted from a general journal. Some systems might also include revenue journals, expenditure journals or a host of subsidiary ledgers and records. For simplicity, the discussion assumes that only the basic books of record are maintained, and that the necessary accrual adjustments (recording receivables and payables of the program) are effected by general journal entry.

- **Cash Receipts Journal**

  The cash receipts journal, as the name implies, is used to records individual amounts received in cash, by date, amount, and source. In other words, the cash receipts journal should indicate the source of the amounts received ("who"), how much was received ("what"), and the date received ("when"). Individual cash receipt ticket numbers are helpful, though not essential, in providing an adequate "audit trail" for later reference.

The 1997 Handbook illustrates a simple form (Exhibit A-26) to capture and accumulate cash receipts information. It is included in the exhibits section for reference.
While the exhibit requires and utilizes all the essential information required to journalize cash receipts, one significant point is brought to the participants' attention. **The Handbook exhibits are not substitutes for the grantee's basic records**. In other words, using the Handbook exhibits does not eliminate the need to record transactions in the grantee's basic records in the same manner as any other transactions.

In this case, the cash receipts journal exhibit is recommended for program purposes, but the grantee should proceed to record the grant amounts received in its own cash receipts journal, as it does amounts received from other (nongrant) sources of cash.

Exhibit 5 is a sample (manually produced) cash receipts journal for the month of July, 19XX, showing both general fund receipts and LCDBG program grant receipts. It illustrates how totals are accumulated from the cash receipts journal, for end of month posting to the general ledger.

It is also acceptable to maintain a separate cash receipts journal for each individual fund (which is typical in computer-based systems). If that were done, there would be individual cash receipts journals for the general fund, LCDBG capital projects fund, and any other funds of the grantee.

- **Cash Disbursements Journal**

Again, as the name implies, the cash disbursements journal captures essential information regarding payments of cash. The 1997 Handbook includes a sample cash disbursements journal for program use (Exhibit A-27), included in the exhibits. It does not accomplish the task of the grantee's basic records.

The essential elements of the cash disbursements journal are the payee ("who"), amount ("what"), date ("when"), check number ("where"), and distribution ("why"). An illustrative manual cash disbursements journal for the same month as the cash receipts illustration is presented as Exhibit 6. It shows how totals are accumulated for end of month posting to the general ledger.

- **General Journal**

The general journal is used to record transactions outside the other journals in use, as well as to record any miscellaneous adjustments necessary from time to time. For example, if in reconciling the checking account, the bank included a debit memorandum for check printing charges, the general journal could be used to record the charge. An illustrative general journal for the same month is presented as Exhibit 7. Also included in the illustration are entries to record LCDBG drawdowns (entry #2) not yet received and LCDBG program expenditures (entry #3) incurred but not paid as of the end of the month, to reflect the accounting on the modified accrual basis.

- **General Ledger and Trial Balance**

The general ledger is where the amounts from the cash receipts and cash disbursements journals are posted, along with general journal entries made during the month.

In some computer-based systems, it may be a *detailed* general ledger, which would show individual receipts and disbursements in each account included in the chart of accounts. The illustration of a manual system includes only the totals from the respective cash journals, and the general journal entries, with a posting reference, which allows the user to find the details of the posting by referring to the journal indicated.

The individual general ledger account pages applicable to the LCDBG program have been reproduced. Following the principles of fund accounting, there should be a separate general ledger for each fund of the governmental entity, including the capital projects fund.

Each general ledger must be self-balancing at all times. The LCDBG general ledger, the general fund general ledger, as well as any other general ledgers for other activities the entity may have, must each "stand alone", that is, they should each reflect equal debits and credits without the accounts of any other fund's general ledger. Exhibits 8 (A-F) are presented for the LCDBG activity in the illustration.

Most computer-based general ledger systems commercially available will not allow the user to make out-of-balance entries, nor will they allow entries that do not balance within each individual funds. However, when a manual system is in use, it is necessary for the accounting personnel to ascertain that after each posting or series of postings that the individual general ledgers are in balance. This may be accomplished by preparing a calculator tape of the account balances included in each general ledger, adding the debits and subtracting the credits. The sum of the entries should thus be zero. An alternative to that approach is to prepare a *trial balance* of the accounts of each fund. A trial balance is simply a list of the individual account balances indicating the fund name, date of the trial balance, and account balance (either debit or credit) at that date. An illustrative trial balance for the LCDBG program capital projects fund as of July 31, 19XX, is included as Exhibit 9. Use of the trial balance facilitates the preparation of financial statements for the various funds of the governmental unit.

- **Budgetary Integration**

As discussed previously, capital projects funds are not required to establish annual operating budgets under either generally accepted accounting principles or under state law. However, a project budget (which covers the entire project, regardless of the time period) is essential in controlling project costs and assessing performance. It is helpful in that respect to integrate the project budget with the accounting records (the general ledger). The general ledger illustrated in both Exhibit 8 and in the comprehensive case study at the end of this text will illustrate how to integrate the project budget in the grant records.

Integration of the budget with the accounting records also facilitates preparation of the Budget Reconciliation Report (1997 Handbook Exhibit A-50). This form is required to be filed with OCD six months after the first drawdown and every six months thereafter.

- **Financial Statements**

At month end, the government should prepare financial statements of its various funds. The basic financial statements of a governmental fund activity (such as a capital projects fund) are the balance sheet and the statement of revenues, expenditures and changes in fund balance. It is the grantee's responsibility to prepare financial statements in accordance with GAAP **each month**. OCD will review the monthly financial statements upon monitoring.

A useful supplementary statement is a cumulative statement of revenues and expenditures compared to budget. This latter statement presents the grant (and any other) revenues as well as expenditures from the beginning of the program to the current period end, and compares them to the program budget. Recognize that this may require the accumulation of amounts outside the current fiscal year. Its purpose is to show how the program is progressing from its beginning to the end of the period, and compare the revenues and expenditures to the program budget on the same basis. Although this statement is not required, it is none the less useful in monitoring program expenditures and identifying cost overruns by line item categories. Further, it is useful in the preparation of the Budget Reconciliation Report discussed in the preceding section.

A balance sheet and statement of revenues, expenditures and changes in fund balance for the LCDBG program capital projects fund are presented as Exhibits 10 and 11. Also presented as Exhibit 12 is the cumulative statement of revenues and expenditures compared to budget. The cumulative amounts represent the current year activity from the basic statement of revenues and expenditures added to the same information for preceding fiscal years. In this case, the entity's fiscal year ends on June 30, and there was LCDBG activity in the preceding year. Those amounts are added together to arrive at the cumulative amounts, which are then compared to the program budget. The budget amounts are derived from the grant document itself, giving effect to any changes approved by OCD.

- **Subsidiary Records**

In addition to the basic journals and the general ledger, some controls are needed to monitor individual contractors and suppliers. These control needs are usually met through the use of subsidiary records such as a vendor payment history commonly found in computer-based systems.

If the system does not provide such, or if a manual system is in place, it will be necessary to establish some vendor history records. The 1997 Handbook provides for the accumulation of the needed information in the "Contract management control card" (Exhibit A-29). A copy of the form is included in the exhibits section for reference. It provides for the subsidiary ledger category (a description of the account from the chart of accounts to which the contractor's payments were charged), contractor name, address, a description of the business (see later discussion of minority/disadvantaged businesses), and the services provided to the program. In addition, it provides space to indicate the date the contractor was cleared to perform services (see later discussion on suspended or debarred parties), the date the contract was executed, date work began, the amount of the contract, and termination date (if applicable).

In the body of the control card, the contractors billings are recorded by invoice date, invoice number, amount and reference (such as "payment request no.6"). Payments to the contractor are recorded by check date, check number, amount, and the billings to date less the payments to date are presented in the "balance" column.

This form serves two other useful purposes. First, it provides an up-to-date history of the billings received from the contractor, in the event of some question regarding the contract, as well as payment history, in the event the contractor inquires as to the status of the account and payment expectations.

Second, the proper use of this form facilitates the preparation of annual information reporting forms required by the Internal Revenue Service (forms 1099). Such reporting is mandatory for unincorporated contractors or service providers when amounts paid to such persons equal or exceed $600 per year. Failure to file and/or provide the 1099's subjects the governmental unit to a penalty of $100 per 1099 not filed or furnished.

Even in computer-based systems providing vendor payment histories, grantees may wish to utilize this form for the reasons cited above.

Internal Control Requirements

What is "internal control"? Internal control is defined as a structure designed to provide management with reasonable (but not absolute) assurance that:

- assets are safeguarded against loss from unauthorized use or disposition, and

- that transactions are executed in accordance with management's authorization and recorded properly to permit the preparation of financial statements in accordance with generally accepted accounting principles.

The concept of *reasonable assurance* acknowledges that internal control is never perfect. Even when internal control is effective , errors and irregularities may still occur and not be detected. Without effective controls, however, the likelihood of errors or irregularities occurring is increased to an unacceptable level. Internal control is defined as a *process,* effected by all levels of personnel, designed to provide reasonable assurance regarding the achievement of objectives in the following categories:

? reliability of **financial reporting**

? effectiveness and efficiency of **operations**

? **compliance** with applicable laws and regulations

The process consists of five interrelated components:

- The **control environment** sets the tone of an organization, influencing the control consciousness of its people. It is the foundation for all other components of internal control, providing discipline and structure. Control environment factors include:

  ? integrity and ethical values

  ? a commitment to competence

  ? participation by the board of directors or audit committee

  ? management's philosophy and operating style

  ? organizational structure

? assignment of authority and responsibility

? human resource policies and practices

? **Risk assessment** is the entity's identification and analysis of relevant risks to achievement of its objectives, forming a basis for determining how the risks should be managed. For example, it may address how the entity considers the possibility of unrecorded transactions or identifies and analyzes significant estimates recorded in the financial statements. Risks can arise or change due to circumstances such as:

? changes in the operating environment

? new personnel

? new or modified information systems

? rapid growth

? new technology

? new lines, products or activities

? corporate restructuring

? foreign operations

? accounting pronouncements

- **Control activities** are the policies and procedures that help ensure that management directives are carried out. Generally, control activities that are relevant to the financial statement audit include

? performance reviews

? information processing

? physical controls

? segregation of duties

- **Information and communication** are the identification, capture and exchange of information in a form and time frame that enable people to carry out their responsibilities. The information system relevant to financial reporting objectives consists of the methods and records established to record, process, summarize and report entity transactions and to maintain accountability for the related assets, liabilities and equity. Communication involves providing an understanding of individual roles and responsibilities pertaining to internal control over financial reporting.

- **Monitoring** is a process that assesses the quality of internal control performance over time. Management monitors controls to consider whether they are operating as intended and that they are modified as appropriate to financial reporting.

The **objectives** and **components** are directly related. The objectives are what an entity strives to achieve (what), while the components are what is needed to achieve the objectives (how).

The five control structure elements are applicable to every audit of every entity, but should be considered in the context of the entity's size, organization and ownership characteristics, nature of the entity's business, diversity and complexity of the operations, methods of transmitting, processing, maintaining and accessing information, and the applicable legal and regulatory requirements.

No matter how well designed and operated, internal control can only provide reasonable assurance regarding the achievement of management's objectives. Limitations will always exist, including the presence of human judgment resulting in simple error or mistake. In addition, controls can be circumvented by collusion of two or more individuals or management override.

Small to medium sized entities may use less formal means to ensure that internal control objectives are achieved. For examples, such entities, generally having active involvement by management in the financial reporting process, may not have extensive descriptions of accounting procedures, sophisticated information systems or written policies. For example a small entity may not have a written code of conduct. Instead, they develop a culture that emphasizes the importance of integrity and ethical behavior through oral communication and management example. Where small entities are involved in large complex transactions or where they are subject to rigorous legal or regulatory requirements, more formal means of ensuring that internal control objectives are achieved may be present.

Office of Community Development Required Policies and Procedures

The OCD has established certain standards and control activities as minimums for administering LCDBG program funds, which are included in the program administration guidelines in the 1997 Handbook. These are summarized in the following paragraphs.

- Once the LCDBG contract has been approved, it must be signed after a thorough reading by the grantee, and returned to the OCD for the appropriate officials' signatures. The contract is not fully executed until all required signatures are affixed.

- Two **Authorized Signature Cards** (1997 Handbook Exhibit A-1) must be completed with original signatures and without erasures or corrections. This card advises the state what persons are authorized to sign the grantee's Requests for Payment.

- In addition, a **Designation of Depository Form** (1997 Handbook Exhibit A-2) must be completed, to provide the OCD with information necessary to accomplish direct deposit of program funds with the financial institution of the grantee's choice. The depository institution must be insured by the FDIC, and the grantee must establish a separate account for the LCDBG program funds. This account may not bear interest, or the amount of interest earned must be returned to the OCD.

- Once the Notice of Removal of Contract Conditions has been received, the grantee may request funds, using the **Request for Payment** form (1997 Handbook Exhibit A-3). The form must be completed accurately, numbered sequentially and signed by those individuals designated on the Authorized Signatory Card. Minimum requests are $3,000 for housing rehabilitation grants and $5,000 for all other grants, unless you have less than those amounts remaining on your contract. The maximum number of requests per month is three for housing rehabilitation grants and two for all other grants.

  Payment requests (or "drawdowns") can normally be made only in amounts needed to satisfy the current disbursement needs, generally the amount to be disbursed within three days of receipt of payment. (An exception is made for disbursements totaling less than certain minimums.) It takes approximately fifteen days to process a request for payment.

- Grantees must generally disburse all LCDBG program funds received within three days of receipt. In cases where the minimum drawdowns are requested (either $3,000 or $5,000), at least one disbursement must be made within the three days. Accordingly, LCDBG funds on hand after disbursements are made should never exceed the minimum amounts of $3,000 or $5,000.

- **One individual must be designated to review and approve all LCDBG transactions**. That individual is responsible for approving purchase orders and contracts funded by LCDBG monies, receive and approve invoices, review and approve requests for payment.

- **A separate governmental fund type must be established to account for the LCDBG program**. As has been discussed, a capital projects or special revenue fund is deemed to be most appropriate for this purpose. The separate fund should record all LCDBG program transactions (including any state or local matching funds) using the modified accrual basis of accounting. The grantee should prepare a balance sheet and statement of revenues, expenditures and changes in fund balance at the end of each month for this fund.

- **The recipient must maintain the books and records of the LCDBG program in the same manner as it maintains the books and records for its other activities**. It is not relevant that a consultant or engineer maintains books and records for the program.

In addition to the above, OCD has established the following minimum requirements regarding segregation of duties:

- **No individual shall have complete control over all phases of any significant transaction**. In other words, the same person cannot authorize payment, record transactions, and sign checks.

- **Record keeping must be separate from operations and the handling and custody of assets**.

- **Monthly reconciliations and verifications of cash balances with bank statements shall be made by employees who do not handle or record cash, or sign checks**.

- **Actual lines of responsibility shall be clearly established and adhered to as closely as possible**.

- **Persons preparing payrolls should not handle the related paychecks**.

- **All persons who handle financial transactions shall be bonded in accordance with state law**.

In some governments, there are too few employees to meet requirements 2 through 5. Officials of those governments should contact OCD for additional guidance in establishing appropriate control policies and procedures specific to their governments. In many cases, it is possible to use elected officials (such as the mayor, one or more aldermen, police jurors, etc.) to meet the requirements.

The **Chart of Accounts** presented in the 1997 Handbook (Exhibit A-25) must be established to account for LCDBG program funds within the capital projects or special revenue fund. A complete discussion of the chart of accounts, with an explanation of the purpose and nature of each account follows.

General Ledger Chart of Accounts

Assets

Account Name	Normal Balance	Nature and Purpose
Cash	Debit	To reflect the beginning and ending balances in the LCDBG checking account, as well as all deposits and disbursements of LCDBG program funds
Grant Revenue Receivable	Debit	To reflect amount due the program, but not yet received as of the end of any period
Accounts Receivable	Debit	To reflect any other amounts due the program but not collected as of the end of any period
Other	Debit	To record any miscellaneous assets of the program not accounted for in other asset accounts

Liabilities

Account Name	Normal Balance	Nature and Purpose
Accounts Payable	Credit	To reflect amounts owed to vendors and suppliers which have not been paid as of the end of any period
Contracts Payable	Credit	To reflect amounts due contractors which have not been paid as of the end of any period
Accrued Salaries	Credit	To reflect amounts due to employees whose salaries are charged to LCDBG program activities which have not been paid as of the end of any period
Unearned Revenue	Credit	To reflect amounts received from the LCDBG program which are not obligated, but were required to meet the minimum drawdown requirements

Account Name	Normal Balance	Nature and Purpose
Other	Credit	To record any miscellaneous liabilities not accounted for in any other liability account
Due to Other Funds	Credit	To account for amounts advanced to the LCDBG program from other activities of the government

Fund Balance

Fund Balance	Credit	To record the excess of revenues over expenditures at the end of the fiscal year

Expenditures

Administration Acquisition Engineering Construction	Debit	To record expenditures of the LCDBG program in the named category

Note that other categories of expenditures may be required depending on the purpose of the grant. A specific account should be established for each line item in the approved grant document. The numbering sequence should be similar for any added accounts.

Revenues

LCDBG Revenues LCDBG Program Income Local Contribution Other Revenue	Credit	To record revenues of the LCDBG program from the named sources

Note that it is possible that other revenue sources will exist. Should additional accounts be required, the numbering sequence should be similar.

OCD requires that the records maintained by the grantee include the books of original entry (the cash receipts and cash disbursements journals), the books of final entry (the general ledger and the **LCDBG Property Register**), and subsidiary records (the contract management control card). The LCDBG Property Register (1997 Handbook Exhibit A-28) is used to record the acquisition and disposition of land, buildings, fixtures, equipment or furniture acquired with program funds. It is required in addition to the basic books of record described above. **It is also required in addition to any existing fixed asset inventory maintained under other state laws**.

The reason the property register is required is to comply with federal requirements (which will be discussed later) for tracking the property acquired with federal funds, its acquisition cost, and the percentage of the asset paid by federal funds.

Other General Policies and Procedures

The following general guidelines and operating policies and procedures are required in the 1997 Handbook:

- **All administrative costs must be charged to "administration"**, and not to other expenditure accounts, such as rehabilitation, sewer, etc.

- **Accounting records must reflect each individual transaction**. Every invoice should be recorded as an expenditure as soon as it is received.

- **Accounting records must be supported by adequate source documentation**. Invoices, purchase orders, vouchers, payrolls, deposit slips, canceled checks, bank statements, etc., must be secured in order to demonstrate how program funds were spent. Payment should **never** be made without original invoices or vouchers in hand.

- **Payroll charges to the program must be supported by a timesheet for each employee indicating the hours worked on the program for each pay period**. A sample timesheet is presented in the 1997 Handbook (Exhibit A-30).

- **Indirect costs charged to the program must be supported by a written cost allocation plan approved by OCD, and on file in the grantee's office**. Indirect costs will be discussed later in this text.

- **Financial records related to the LCDBG program must be retained for three years after closeout of the program**. In addition, access to those records must be assured to state officials and their representatives, or the U.S. Department of Housing and Urban

Development.

Section IV. Compliance requirements for grant recipients

The Single Audit Act of 1996 (as revised) establishes certain federal laws and regulations as critically important to the administration of federal grants, which include "pass-through" programs such as the LCDBG program. Those laws and regulations are set forth in the (provisional) OMB Circular A-133 Compliance Supplement (the Compliance Supplement). The Compliance Supplement presents fourteen requirements, which apply to all entities.

Each of the fourteen requirements is unique. In order to comply with the requirements it is first necessary to be aware of and understand the provision. Secondly, proper administration of the program requires that specific control activities be established to prevent or detect noncompliance with each of the requirements.

In the remainder of this section, we will discuss each of the fourteen requirements applicable to the LCDBG program. The program is best described in the Compliance Supplement under Catalog of Federal Domestic Assistance (CFDA) Number 14.219, *Community Development Block Grants/Small Cities Program*. This text will consider the types of errors (noncompliance) that could occur, and suggest control activities (policies and procedures) that are believed to be effective in preventing or detecting noncompliance with the requirements.

It is not required that all suggested control policies and procedures be in place in all grantees. To do so, in many small governments, would simply be cost prohibitive. However, some control policies and procedures should be in place for each requirement. The extent of the policies and procedures is a matter of management's judgment, considering the related cost and benefits.

Following this page are the fourteen requirements established by the Compliance Supplement and suggested control activities.

(A) ACTIVITIES ALLOWED OR UNALLOWED AND (B) ALLOWABLE COSTS/COST PRINCIPLES

Compliance requirements - The applicable cost principles, contained in Office of Management and Budget (OMB) Circular A-87, prescribe the cost accounting policies associated with the administration of federal awards by state and local governments (including Indian tribal governments). The circular contains the selected cost items, allowable and unallowable costs, and standard methodologies for calculating indirect cost rates (more information is presented following the fourteen requirements). In addition to the cost principles, regulations applicable to the program establish parameters for use of CDBG funds.

Objectives - To provide reasonable assurance that federal awards are expended only for allowable activities and that the costs of goods and services charges to federal awards are allowable and in accordance with the applicable cost principles. For the LCDBG program, the following guidance is provided in the Compliance Supplement regarding Activities Allowed or Unallowed:

- All activities undertaken must meet one of three national objectives of the CDBG program, i.e.,benefit low- and moderate-income persons, eliminate slums or blight, or meet community development needs having a particular urgency (24CFR Section 570.200).

- CDBG funds are to be used for the following activities: (1) the acquisition of real property, (2) the acquisition, construction, reconstruction or installation of public works, facilities and site, or other improvements, including removal of acrhitectural barriers that restrict accessibility of elderly or severely disabled persons, (3) code enforcement in deteriorated or deteriorating areas, (4) clearance, demolition, and removal of buildings and improvements, (5) payments to housing owners for losses of rental income incurred in temporarily holding housing for the relocated, (6) disposition of real property acquired under this program, (7) provision of public services (subject to limitations contained in the CDBG regulations), (8) payment of the non-Federal share for another grant program that is part of the assisted activities, (9) interim assistance where immediate action is needed prior to permanent improvements or to alleviate emergency conditions threatening public health and safety, (10) payment to complete a Title I Federal Urban Renewal Project, (11) relocation assistance, (12) planning activities, (13) administrative costs, (14) acquisition, construction, reconstruction, rehabilitation or installation of commercial or industrial buildings, (15) assistance to community-based development organizations, (16) activities related to privately owned utilities, (17) assistance to private, for-profit businesses, when appropriate to carry out an economic development project, (18) construction of housing assisted under Section 17 of the United States Housing Act of 1937, (19) reconstruction of properties, (20) direct home ownership assistance to facilitate and expand home ownership (21) technical assistance to public or private entities for capacity building (exempt from the planning/administration cap), (22) housing services related to HOME funded activities, (23) assistance to institutions of higher education to cry our eligible activities, (24) assistance to public and private entities (including for-profits) to assist micro-enterprises, (25) payment for repairs and operating expenses for acquired Ain Rem@ properties, (26) residential rehabilitation including code enforcement, lead-based paint hazard evaluation, and removal (24 CFR Section 570.200-207).

- Each funded activity must meet all of the same requirements that apply to CDBG-assisted activities generally (24 CFR Section 570.301).

- All of the activities that a grantee undertakes during their CDBG program year must be identified in an action plan (24 CFR Sections 91.220 and 570.301).

- CDBG funding can only be used for special economic development projects that meet the criteria in 24 CFR Section 570.203. Grantees must have data to support that assistance provided to carry out special economic development projects is appropriate by meeting the public benefit standards for job creation and provision of goods and services described in 24 CFR Section 570.209.

- When CDBG funds are used to finance rehabilitation, the rehabilitation is to be limited to privately owned buildings and improvements for residential purposes, low income housing public housing and other publicly owned residential buildings and improvements, publicly or privately owned commercial or industrial buildings under certain circumstances, as well as manufactured housing when it is used as part of the community's permanent housing stock (24 CFR Section 570.202).

Types of errors or irregularities that could occur:

- Federal funds may be used in a manner that is inconsistent with the above federal program regulations (and thus not meet one of the three national objectives cited above).

- A nonnallowable cost (one which does not meet the criteria of allowability, reasonableness and allocability) could be charged against a federal program.

- A federal program could bear more than its fair share of indirect costs.

SUGGESTED CONTROL ACTIVITIES - Activities Allowed or Unallowed

? A supervisor's review and approval of all invoices that support charges to a federal program. This review should address whether the charge is in accordance with the federal program regulations and the approved program budget.

SUGGESTED CONTROL ACTIVITIES - Allowable Costs/Cost Principles

? Persons responsible for approving program expenditures are aware of the requirements of OMB Circular A-87 and evaluate program charges based on these criteria.

? A supervisor's review and approval of all invoices that support charges to the program. This review should address whether the charge is in accordance with the approved program budget.

? Utilization of a checklist denoting allowable, unallowable, and possibly unallowable costs by person responsible for approving expenditures charged to the program.

? The entity has prepared a cost allocation plan or indirect cost rate proposal that provides a basis for allocating indirect costs to the program.

? The cost allocation plan/indirect cost rate proposal is supported by documentation that demonstrates that the plan was prepared from accurate financial and reasonable statistical data.

? The cost allocation plan or indirect cost rate proposal has been submitted to and approved by the Office of Community Development.

? Indirect cost charges included as program expenditures are reviewed by supervisory personnel and are determined to be in accordance with the entity's cost allocation plan or indirect cost rate proposal.

? Utilization of an outside expert to prepare or periodically review the indirect cost allocation plan and or adherence to the plan.

(C) CASH MANAGEMENT

Compliance requirements - Whenever cash is advanced, recipients must have procedures in place to minimize the time lapse between the transfer of funds from the Treasury and the actual disbursement of the funds. The Office of Community Development requires that for programs that do not disburse payments until after receipt of Treasury funds should release checks within three banking days of such receipt.

Objectives - To provide reasonable assurance that:

- The draw down of program cash is only for immediate needs.

Types of errors or irregularities that could occur:

- The award recipient could receive program funds before those funds are actually needed to pay expenditures of the program, thus maintaining idle cash balances of program funds.

- The award recipient could unreasonably delay payment of vendors after program funds are received.

SUGGESTED CONTROL ACTIVITIES - Cash Management

? All requests for funds are approved by supervisory personnel. **If the program has been previously monitored, supporting documentation of these expenditures should accompany the request**.. The forms should be reviewed before requests are approved and signed.

? Maintaining a cash log showing expenditures and cash balances for the program.

? Supervisory personnel periodically inspect files of unprocessed invoices to ensure that vendors are paid on a timely basis.

? Supervisory personnel periodically review cash balances of program funds to ensure that cash balances are not excessive.

(D) DAVIS-BACON ACT

Compliance requirements - All laborers and mechanics employed by contractors and subcontractors to work on construction contracts in excess of $2,000 financed by program funds must be paid wages equal or exceeding the amounts established by the United States department of Labor (DOL) for the locality of the project.

Objectives - To provide reasonable assurance that laborers and mechanics employed by contractors and subcontractors are paid at least the prevailing wage rates for projects covered by the Davis-Bacon Act.

Types of errors or irregularities that could occur:

- If applicable, laborers and mechanics working on construction projects financed by federal funds could be paid wages less than those established for the locality by the Department of Labor.

SUGGESTED CONTROL ACTIVITIES - Davis-Bacon Act

? Applicable construction contracts contain provisions requiring the payment of "prevailing wages".

? When requests for payments are made by contractors, the contractors are required to provide detail on all labor costs that includes the employee's name, job classification, and wage rate. Reported wage rates are compared to prevailing wage rates established by the Secretary of Labor before the request for payment is approved.

? Interviews with contractor's laborers to verify their wage rates and comparing them to the prevailing wage rates.

? Posting prevailing wage rates and the provisions of the Davis-Bacon Act at the job site.

? Assign responsibility to monitor contractors for compliance with the contract terms, including Davis-Bacon provision.

(E) ELIGIBILITY

There are no eligibility requirements applicable to the program.

(F) EQUIPMENT AND REAL PROPERTY MANAGEMENT

Compliance requirements - equipment management

Title to equipment (tangible nonexpendable property with a useful life of more than one year and costing $5,000 or more) acquired with program funds rests with the award recipient. Award recipients must follow state laws for equipment acquired. Likewise, local governments and tribal governments must follow the A-102 Common Rule for equipment acquired under awards received. Circular A-102 requires that the equipment be used in the program which acquired it (or when appropriate, other federal programs). Equipment records are required to be maintained, and physically inventoried at least every other year. The inventory must be reconciled to equipment records, and appropriate controls must be established. Equipment must be adequately maintained.

When equipment is no longer needed, it may be retained or sold. The awarding agency is entitled to its proportionate share of the fair market value. Proper sales procedures must be followed in the disposition of equipment acquired by federal funds, including competitive bidding to the extent practicable.

Compliance requirements - real property management

Similarly, title to real property acquired with program funds remains with the recipient. Real property must be used for its authorized purpose until it no longer needed for that purpose. Entities may not dispose of the real property without prior consent of the awarding agency.

When no longer needed, the recipient must request disposition instructions from the awarding agency. When the property is sold, competitive bidding practices must be followed to ensure the highest price is obtained. If sold, recipients are normally required to remit the awarding agency's proportionate share of the proceeds. If the property is not sold, the recipient must compensate the awarding agency for its proportionate share of the fair market value. In some cases, disposition instructions may provide for a transfer of title to another entity, in which case, the recipient is entitled to compensation for the nonfederal share of the property's fair market value.

Objectives - To provide reasonable assurance that:

- proper records are maintained for equipment and real property acquired with federal funds
- equipment and real property is adequately safeguarded and maintained
- disposition or encumbrance of any equipment or real property is in accordance with federal

requirements

- the awarding agency is appropriately compensated for its share of any property sold or otherwise converted to nonfederal use.

Types of errors or irregularities that could occur:

- Equipment or real property acquired with federal funds might be disposed of without proper authorization and return of applicable funding to the appropriate agency

SUGGESTED CONTROL ACTIVITIES - Equipment and Real Property Management

? Maintenance of real property records.

? Existence of fixed asset inventory system.

? Periodic reviews to ensure real property is used for authorized purposes.

? Assignment of responsibility for obtaining disposition instructions for real property and disposing of real property no longer needed for the authorized purposes.

? Documentation of federal requirements relating to the frequency of conducting inventory (every two years), transfer, property utilization, property disposition, and accounting.

(G) MATCHING, LEVEL OF EFFORT, EARMARKING

Compliance requirements - **Matching** includes requirements to provide nonprogram contributions of a specified amount or percentage to match program awards. Matching may be in the form of cash or in-kind contributions. Although the program regulations do not establish matching requirements, those requirements may be included as part of the program budget, and are therefore required by contract. If so, the following guidance if provided from the Compliance Supplement on matching funds.

Acceptable matching amounts are:

- verifiable from the entity's records
- not included as contributions for any other program
- necessary and reasonable
- allowable under the applicable cost principles
- not paid by the federal government under another award
- provided for in the approved budget
- conform to other applicable provisions

.

Compliance requirements - Level of effort There are no level of effort requirements applicable to the program.

Compliance requirements - Earmarking includes requirements that specify the minimum and/or maximum amount or percentage of the program's funding that must or may be used for specified activities. The following earmarking requirements apply to the program:

- Not less than 70 percent of the program funds must be used for activities that benefit low and moderate income persons. In determining the benefit to such persons, the criteria in 24 CFR Sections 570.420(e) and 570.430(e) are used.

- Not more than 20 percent of the total grant plus 20 percent of the program income received during a program year may be obligated during that year for activities that qualify as planning and administration pursuant to 24 CFR Sections 570.205 and 570.206.

- The amount of program funds obligated during the program year for public services must not exceed 15 percent of the grant amount received for that year plus 15 percent of the program income it received during the preceding program year.

Objectives - To provide reasonable assurance that matching and earmarking requirements are met using only allowable funds or costs which are properly calculated or valued.

.

Types of errors or irregularities that could occur:

- State or local matching funds that are required to be used in the program are not being so used.

- Program expenditures financed with state or local matching funds do not meet the required allowability and allocability standards applied to other program expenditures.

- The recipient has not maintained the earmarking requirements with respect to low and moderate income benefits, administration and public services.

SUGGESTED CONTROL ACTIVITIES - Matching, Level of Effort and Earmarking

? Program budgets include state or local funds match in budgeted revenues.

? State or local funds to be used for matching in the program are appropriated in the recipient's operating budget for such match requirements.

? Expenditures that are paid with state or local funds but which are used to meet matching requirements in the program are subjected to the same review and approval process for other program expenditures.

? Actual program revenues and expenditures are compared to budgeted revenues and expenditures on a periodic basis to ensure that local support is in accordance with earmarking requirements.

(H) PERIOD OF AVAILABILITY OF FUNDS

Compliance requirements - Awards may specify a time period during which the recipient may use its program funds. Where a funding period is specified, the entity may only charge to the award costs resulting from obligations incurred during the funding period (and any authorized pre-award costs). In some cases, the Office of Community Development may authorize the recipient to carry over any unobligated balances to the subsequent funding period. AObligations@ means the amount of orders placed, contracts and subcontracts awarded, goods and services received, and similar transactions during a given period.

Recipients must liquidate obligations incurred under an award within 90 days after the end of the funding period, in order to coincide with the submission of the annual financial status report (form SF269). The Office of Community Development may extend this deadline upon request.

Objectives - To provide reasonable assurance that program funds are used only during the authorized period of availability.

Types of errors or irregularities that could occur:

- Federal funds could be used outside the period for which they were intended.

SUGGESTED CONTROL ACTIVITIES - Period of availability of funds

? Review of expenditures to ensure charges result from obligations of the funding period unless carryover of unobligated balances is permitted.

? Assignment of responsibility to liquidate all obligations incurred under the award no later than 90 days after the end of the funding period.

? Use of checklist to ensure liquidation of obligations and submission of annual Financial Status Report.

(I) PROCUREMENT AND SUSPENSION/DEBARMENT

Compliance requirements - procurement

Recipients must use the same policies and procedures for procurement of CDBG funded activities as they use for nonfederally funded activities. In addition, they must ensure that purchase orders and other contracts include clauses required by federal statutes and executive orders and their implementing regulations.

Compliance requirements - suspension and debarment

Recipients are prohibited from contracting with or making subawards under Acovered transactions@ to parties who are suspended or debarred or whose principals are suspended or debarred. The term Acovered transactions@ means contracts for goods or services equal to or above $100,000 and <u>all</u> nonprocurement transactions (subawards).

Objectives - To provide reasonable assurance that:

- The procurement of goods and services are made in compliance with the provisions of applicable law

- No subaward, contract or agreement for the purchase of goods or services is made with any debarred or suspended party

Types of errors or irregularities that could occur:

- Procurement may be made which does not follow the applicable requirements.

- Parties who are suspended or debarred may be contracted to provide goods or services under federal awards.

SUGGESTED CONTROL ACTIVITIES - Procurement and Suspension/Debarment

? Incorporation of federal procurement standards in the entity's purchasing policy.

? Review of purchase requisitions or purchase orders by person knowledgeable of procurement requirements.

? Assignment of responsibility to ensure that awards are not made to any debarred or suspended parties.

(J) PROGRAM INCOME

Compliance requirements - AProgram income@ means gross income received that is directly generated by the federally funded project during the grant period. When authorized, costs incident to the generation of program income may be deducted from gross income to arrive at program income. Program income includes (but is not limited to) income from fees or services performed, use or rental of real or personal property, sale of commodities or items acquired or fabricated under federal awards, payments of principal or interest on loans made with grant funds. Unless specifically stated in the award agreement, program income does not include interest on grant funds (covered under cash management requirements), rebates, credits, discounts, refunds (covered under allowable costs/cost principles) or interest earned on any of them (covered under cash management). Program income does not include the proceeds from the sale of equipment or real estate (covered under equipment and real property management).

Program income may be used in one of three ways:

- deducted from outlays
- added to the project budget
- used to meet matching requirements

Unless specified in the terms of the award, program income must be deducted from outlays.

Objectives - To provide reasonable assurance that program income is correctly earned, recorded and used in accordance with program requirements.

Types of errors or irregularities that could occur:

- Program income may be used in a manner inconsistent with federal requirements.

SUGGESTED CONTROL ACTIVITIES - Program Income

? Establishment of records to track program income.

? Assignment of responsibility for ensuring that current program income is deducted from current allowable costs in determining federal drawdowns or reimbursements.

? Assignment of responsibility to ensure that program income is used only in an authorized manner

(K) REAL PROPERTY ACQUISITION AND RELOCATION ASSISTANCE

Compliance requirements - The Uniform Relocation Assistance and Real Property Acquisition Policies Act of 1970 (the Act) provides for uniform and equitable treatment of persons (and businesses) displaced from their homes, businesses and farms by federally funded programs. The Act requires that property be appraised in the presence of the owner by qualified independent appraisers. All appraisals must be examined by a review appraiser to assure acceptability. Upon acceptance, the review appraiser certifies the recommended or approved value of the property to establish the offer of just compensation to the owner. Federal requirement govern the determination of payments for replacement housing assistance, rental assistance, and down payment assistance for those displaced by acquisitions under federally funded programs. Also addressed in regulation are the payment of moving-related expenses and reestablishment expenses incurred by displaced businesses and farms.

Objectives - To provide reasonable assurance of compliance with:

- property acquisition, appraisal, negotiation and residential relocation requirements
- replacement housing payment requirements
- rental or down payment assistance requirements
- business relocation and reestablishment payment requirements

Types of errors or irregularities that could occur:

- Real property acquisitions could be handled in such a manner that property owners are not compensated fairly for their property.
- In the case of relocations, the property owners would not receive assistance in relocating and may not be able to obtain adequate replacement property.

SUGGESTED CONTROL ACTIVITIES - Relocation Assistance and Real Property Acquisition

? A real property acquisition policy that contains the following provisions:

a. Property is appraised in the presence of the owner.

b. All appraisals will be reviewed.

c. Price is set based on appraisals.

d. Settlements are negotiated with the owners in a manner that is fair to both parties.

? A relocation assistance policy that contains the following provisions:

a. Assistance is provided to displaced individuals in locating replacement housing.

b. Replacement property shall meet acceptable standards.

c. Adequate recordkeeping will be maintained on all relocations.

? The existence of a "relocation officer", i.e., the assignment of a person to monitor compliance with program requirements.

? Use of a checklist of federal requirements by persons responsible for administering programs involving relocation or real property acquisition.

? Practice of sending information to persons being relocated, informing them of their rights and the prescribed procedures.

- Practice of requesting written acknowledgement of persons being relocated that the required procedures and rights were made available to them.

? Existence of a review function over the acquisition of real property for compliance with federal requirements.

(L) REPORTING

Compliance requirements - Standard reporting forms should be used. These may require financial, performance or special reporting information. Each recipient must report program outlays and income on the modified accrual basis as prescribed by the Office of Community Development.

Recipients must submit Performance and Assessment Reports at least annually, but not more frequently that quarterly. Performance reports generally contain brief information on each of the following:

- a comparison of actual performance with the goals and objectives established for the period
- the reasons why goals were not met, if applicable
- other information, including analysis and explanation of cost overruns or high unit costs

Objectives - To provide reasonable assurance that reports of federal awards submitted:

- include all activity of the reporting period
- are supported by underlying accounting or performance records
- are fairly presented in accordance with program requirements

Types of errors or irregularities that could occur:

- The required reports may not be submitted on a timely basis.
- The reports may contain inaccurate information.

SUGGESTED CONTROL ACTIVITIES - Reporting

? Employees responsible for preparing federal financial reports are provided a timetable with dates the reports are due.

? Reports are prepared from reliable accounting data, and on the modified accrual basis.

? Supervisory personnel (other than preparers) are responsible for reviewing and signing reports. This review should include a determination that the report is filed on a timely basis and that the information in the report is supported by the accounting records.

? Periodic documented reconciliations of financial reports to the general ledger.

(M) SUBRECIPIENT MONITORING

The subrecipient monitoring provisions are not applicable to the program.

(N) SPECIAL TESTS AND PROVISIONS

Compliance requirements -

Citizen participation - Recipients must adopt a citizen participation plan and certify to the Office of Community Development that the citizen participation requirements of 24 CFR Sections 91, 570.301 and 570.431, as applicable, have been met.

Request for Release of Funds (RROF) and environmental certification - Program funds cannot be obligated until the Request for Release of Funds (RROF) has been approved.

Environmental reviews - Projects must have an environmental review unless they meet criteria specified in the regulations that would exclude them from RROF and environmental certification requirements.

Rehabilitation - When program funds are used for rehabilitation, the recipient must assure that work is properly completed and meets local codes.

Objectives - To provide reasonable assurance that the special provisions described above have been met.

Types of errors or irregularities that could occur:

- The recipient may not be in compliance with special requirements contained in program legislation.

SPECIFIC CONTROL ACTIVITIES - Special Tests and Provisions

? Persons responsible for administering the program have copies of and are aware of the above special provisions contained in the OMB's Compliance Supplement.

? Grant agreements are reviewed for special provisions and procedures are documented that address how special compliance provisions will be satisfied.

OMB CIRCULAR A-87 - COST PRINCIPLES APPLICABLE TO RECIPIENTS

The office of Management and Budget has revised Circular A-87, *Cost Principles for State, Local and Indian Tribal Governments,* generally effective for awards (including continuation or renewals) after September 1, 1995.. The previous version, issued in January 1981, is rescinded. Some of the changes have been made to enhance clarity and readability, while others are substantive. The new Circular consists of five attachments (A through E), which are summarized below.

Attachment A - General Principles for Determining Allowable Cost

Purpose and Scope

The Circular is intended to establish principles to determine allowable cost incurred by state, local and tribal governments under grants, contracts and other agreements with the Federal government. It is not intended to identify circumstances or dictate the extent of involvement of the Federal government in a particular project or activity. The Circular exists to provide that Federal programs bear their fair share of the costs recognized under a program. Provision for profit or other increment above cost is not addressed by the Circular.

The application of the cost principles is based on the premises that:

- Governmental units are responsible for the efficient and effective administration of Federal awards through sound management;

- Governmental units assume responsibility for administration in a manner consistent with underlying agreements, program objectives, as well as the terms and conditions of the Federal award programs;

- Each governmental unit, in recognition of its unique combinations of staff, facilities and experience, will have the primary responsibility for employing whatever form of organization and management techniques may be necessary for proper and efficient administration of the Federal award.

The principles are to be applied by all Federal agencies in determining allowable costs, other than for entities under Circular A-21, and health care providers who are subject to requirements promulgated by sponsoring Federal agencies. Subawards are subject to the cost principles applicable to the particular organization concerned, i.e., if the subaward is made to a college or university, the principles of Circular A-21 will apply; subawards to nonprofit organizations are subject to the principles of Circular A-122.

Definitions

Selected definitions are presented below.

Approval or authorization of the awarding or cognizant Federal agency - documentary evidence of consent prior to incurring a specific cost, such as the cost being specifically identified in the Federal award document, or inclusion in a state/local wide cost allocation plan which has been approved.

Award - grant, cost reimbursement contract or other agreement between a state/local or tribal government.

Awarding agency - for direct awards, the Federal agency; for subawards, the party that awarded the subaward (the primary recipient).

Cognizant agency - the agency responsible for reviewing, negotiating and approving cost allocation plans or indirect cost proposals under the Circular for all agencies. OMB publishes a list of cognizant agencies.

Cost - the amount determined on the cash, accrual or other basis acceptable to the Federal awarding agency or cognizant agency.

Cost allocation plan - any of three specific types of plans:

> **Central services cost allocation plan** - the documentation identifying, accumulating and allocating or developing billing rates, based on the allowable costs of services provided by a governmental unit on a centralized basis to its departments and agencies. These costs may be allocated or billed to users.
>
> **Public assistance cost allocation plan** - a narrative description of the procedures that will be used in identifying, measuring and allocating all administrative costs to all of the programs administered or supervised by state public assistance agencies as described in Attachment D of the Circular.
>
> **Indirect cost rate proposal** - documentation prepared by a governmental unit (or a component unit) to substantiate its request to establish an indirect cost rate under Attachment E of the Circular.

Basic Guidelines

To be allowable under the Circular, costs must meet the following criteria:

- **Be reasonable and necessary** for the proper and efficient performance and administration of the program;
- **Be allocable to Federal awards** under the Circular;
- **Be authorized and not prohibited** under state or local laws or regulations;
- **Conform to limitations or exclusions** set forth in the cost principles, Federal law, terms and conditions of the award program, or other governing regulations;
- **Be consistent with policies and procedures** that apply uniformly to both Federal and nonfederal activities;
- **Be afforded consistent treatment** and not treated as both direct and indirect cost;
- **Be determined in accordance with GAAP** except as provided otherwise;
- **Not be used to meet matching or other requirements**;
- **Be net of applicable credits**;
- **Be adequately documented**.

Further guidance is provided on the following matters:

Reasonable costs are those that do not exceed the amount that would have been incurred by a prudent person under the circumstances that prevailed at the time the decision was made to incur the cost. Consideration should be given to (1) whether the cost is of a type that is generally recognized as ordinary and necessary for operation of the program, (2) sound business practices, arm's length bargaining, terms and conditions of the award, (3) market prices for comparable goods and services, (4) whether the individuals involved acted prudently, and (5) significant deviations from established practices which may have increased the Federal award's cost.

Allocable costs must be chargeable to a particular cost objective in accordance with the relative benefits received by that objective. All objectives which receive benefit from a particular indirect cost must receive an appropriate allocation of indirect costs. Costs allocable to a particular cost objective may not be charged to another cost objective to overcome fund deficiencies, avoid restrictions imposed by law or terms of the Federal award or for any other reason. Whenever indirect costs are ultimately charged to a Federal program, a cost allocation plan is required.

Applicable credits refer to those receipts or reductions of expenditure transactions that offset or reduce expense items allocable to Federal awards as either direct or indirect costs. Examples include purchase discounts, rebates, recoveries or indemnities on losses, insurance refunds or rebates, adjustments of overpayments or erroneous charges. Such items allocable to a Federal award must be credited as either a cost reduction or cash refund.

Composition of cost

Total cost includes the allowable direct cost plus allocable indirect costs, less applicable credits.

Direct costs typically include:

> Compensation for employees for the time devoted and specifically identified to the performance of an award;
>
> Materials acquired, expended or consumed for the purpose of the awards;
>
> Equipment and other approved capital expenditures;
>
> Travel expenses incurred specifically in carrying out the program.

Minor directs costs may be treated as indirect costs for practical reasons, as long as such costs are treated consistently.

Indirect costs are those which are:

> Incurred for a common or joint purpose, benefitting more than one cost objective;
>
> Not readily assignable to the cost objectives specifically benefitted without effort disproportionate to the results achieved.

Interagency services are those provided by one agency to another within the governmental unit, and may include direct costs of the service provided and allocable indirect costs. A standard indirect cost allowance of ten percent of the direct salary and wage cost (excluding overtime, shift differentials, and fringe benefits) may be used in lieu of determining the actual indirect costs of the service. These services do not include centralized services included in central service cost allocation plans.

Required certifications must be made for each cost allocation plan or indirect cost rate proposal using the Certificate of Cost Allocation Plan or Certificate of Indirect Costs as set forth in Attachments C and E. These must be signed on behalf of the governmental unit by the chief financial officer (or someone of higher position). No plan or rate shall be approved unless the plan or rate has been certified. In cases where no certification is provided, the Federal government may either disallow all indirect costs or unilaterally establish such a plan or rate, based on audited historical data or other information furnished to the cognizant agency. Such a plan will ensure that nonallowable costs have been excluded.

Attachment B - Selected Items of Cost

Sections 1 through 42 of Attachment B provide principles to be applied in establishing the allowability or unallowability of certain items of cost, which principles apply to both direct and indirect costs alike. **Items not addressed in Attachment B are not necessarily allowable or unallowable; rather, the principles should be used to make the determination, based on the treatment or standards for similar items of cost**.

The following is an abbreviated summary of the costs which are allowable, allowable with advance approval, and unallowable under Attachment B:

<u>Allowable</u>

Accounting	Establishing and maintaining accounting and information systems.
Advertising	Costs related to personnel recruitment, procurement of goods and services, disposal of surplus materials, or other specific purposes necessary to meet award requirements (and not prohibited below).
Audit services	Provided the audit meets the requirements of Circular A-133 the cost is allowable. The percentage of audit costs charged to the Federal awards is determined by the ratio of Federal expenditures to total expenditures for the year, <u>unless appropriate documentation demonstrates a higher actual cost</u>.
Automatic data processing	(But see below regarding equipment and other capital expenditures.)
Bonding costs	Allowable to the extent in accordance with sound business practice.
Budgeting	Includes development, preparation, presentation and execution.
Communications	Telephone, mail, messenger and similar costs.
Compensation for personal services	Currently paid or accrued, including fringe benefits (such as compensated absences, insurance, pensions and wage continuation plans, and where consistent with the governmental unit's policy), are allowable to the extent they are (1) reasonable (based on similar work in the other activities of the governmental unit, or in the labor market) and conform to policy of the

governmental unit consistently applied, (2) follows an appointment made in accordance with the governmental unit's laws and rules and meets merit system or other requirements required, and (3) is determined and supported as required below.
Salaries and wages are to be supported by documented payrolls approved by a responsible official. No additional documentation is required for employees who work on a single cost objective, other than periodic (at least semiannual) certifications that the employee worked only on that cost objective. For employees who work on multiple cost objectives, the salary distribution should be based on personnel activity reports or equivalent documentation, unless a statistical sampling system or other substitute system has been approved.

The personnel activity reports must (1)reflect an after-the-fact actual distribution of the employees' activity, (2) account for the total of the employees' activities, (3) be prepared at least monthly and coincide with one or more pay periods, and (4) be signed by the employee(s). Budget estimates or percentages determined in advance do not qualify as support, but may be used for interim purposes, provided that (1) the estimates are reasonable, (2) at least quarterly, actual costs are compared to the estimates and adjustments made (this may be done annually, if the comparisons show that the differences are less than ten percent), and (3) estimates or percentages are revised at least quarterly, if necessary, to reflect changed circumstances.

Donated services may be provided by professional or technical persons, consultants and skilled and unskilled laborers. These costs are not reimbursable as either direct or indirect costs, but may be used to meet cost sharing or matching requirements. To the extent possible, donated services should be documented in the same manner as compensated services.

Depreciation and use allowances

Within a single class of assets (buildings, office equipment, computer equipment, etc.) both depreciation and a use allowance cannot be claimed. Depreciation must be based on historical acquisition cost, or if unavailable, estimated historical cost. Donated assets are valued at their fair market value at the time of donation <u>by an unrelated third party</u> (which excludes governmental organizations within the same state).

Depreciation and use allowances must exclude the cost of land, and buildings and equipment, to the extent provided by Federal awards, and any portion contributed by/for the governmental unit in fulfillment of a matching requirement.

Where use allowances are employed, the use allowance for buildings and improvements (e.g.,parking areas, fences and sidewalks) is two percent of acquisition cost. Building components may not be disaggregated from the building's shell, and classified as equipment. In general, equipment is movable without destruction of, or need of costly repairs to, the building. The use allowance for equipment is six and two-thirds percent of acquisition cost.

Where depreciation is charged to a program, the useful life must consider the type of construction, nature of the equipment used, historical usage patterns, technology developments, and the renewal and replacement policy of the governmental unit. In the absence of clear evidence to the contrary, the straight line method must be used. Federal approval is required for any change in depreciation methods.

Component depreciation may be used for buildings. Reasonable use allowances may be negotiated for fully depreciated assets.

At least biennially, an inventory of fixed assets must be taken to ensure that the assets exist and are in use. Historical cost and depreciation records must be maintained.

Disbursing service	Costs of disbursing funds by the treasurer or other officer are allowable.
Insurance	Costs of insurance and indemnification required are allowable.
Maintenance, operations and repairs	To the extent they (1) keep property in efficient operating condition, (2) do not add to the permanent value of property and (3) are not otherwise included in rental and other charges, these costs are allowable.
Memberships	Technical, professional and business organizations are allowable, as are subscriptions to publications of such organizations, and the costs of meeting and conferences for similar purposes (including associated travel).
Materials and supplies	Allowable at net delivered cost, including withdrawals from general stores or stockrooms.
Professional services	Professional and consultant fees for services are allowable, including retainer fees supported by evidence of bona fide services rendered.
Proposal costs	Cost of preparing proposals for potential awards are allowable (usually as indirect costs); if charged directly to an award, advance approval is required.

Publication and printing costs	Such costs, including distribution, promotion mailing and general handling are allowable.
Rearrangements and alterations	Ordinary and normal costs are allowable. Special arrangements and alterations require advance approval.
Rentals	To the extent the rates are reasonable in light of costs of comparable property, market conditions, alternatives available and the type, life expectancy, condition and value of the property leased (assuming arms length transactions).
Taxes	Taxes that a government is legally required to pay are allowable, except self-assessed taxes that disproportionately affect the Federal awards.
Training	Costs of employee development are allowable.
Travel	Transportation, lodging, subsistence, and related items incurred by employees traveling on official business, whether on actual costs, per diem allowances, mileage reimbursement or a combination, provided the same method is used for the entire trip. Reasonableness of these expenses is to consider the normal governmental unit policies and limitations. Airfare must be at the coach rate, unless such fare would (1) require circuitous routing, (2) require travel at unreasonable hours, (3) excessively prolong travel, (4) greatly increase the duration of the flight, (5) result in additional costs that would offset the transportation savings, or (5) not be suitable for the medical needs of the traveler.

Unallowable

Advertising	Costs related to general events of the governmental unit, promotional items and memorabilia, gifts, models, or souvenirs, and general public relations costs are not allowable.
Alcoholic beverages	Not allowable. Period.
Bad debts	Not allowable, unless provided for in program regulations.
Contingencies	Not allowable, with the exception of self-insurance reserves, pension plan reserves and other post-employment benefit reserves computed under acceptable actuarial methods.

Contributions	Not allowable, including cash, property and services, regardless of the recipient.
Defense and prosecution of criminal and civil proceedings and claims	Costs to defend any criminal or civil fraud or similar proceeding brought by the Federal government where the contractor is found liable or pleaded no contest, as well as costs incurred by a contractor in connection with any civil, criminal or administrative proceeding commenced by the Federal government, are not allowable Legal fees required to administer a Federal award are allowable. Legal fees for prosecution of claims against the Federal government are not allowable.
Entertainment	See alcoholic beverages.
Fines and penalties	Nonallowable, unless incurred as a result of compliance with specific provisions of the Federal award or written instructions by the awarding agency in advance.
Fund raising and investment management costs	Fund raising costs are unallowable, regardless of the purpose for which the funds will be used. Investment management costs are unallowable, except to the extent related to pension, self-insurance or other funds which have Federal participation.
General government expenses	Salaries and expenses of the chief executive officer, legislative bodies, judicial activities, prosecutorial activities (unless treated as a direct cost to a specific program where authorized in program regulations), and other general government expenses (such as police and fire protection) are unallowable.
Idle facilities	Unallowable, except to the extent that they are necessary to meet the fluctuations in workload, or result from changes in the program requirements, economy efforts, reorganization or other changes that could not reasonably be foreseen.
Interest	Unallowable, except for costs paid after the effective date of the Circular which are related to otherwise allowable building acquisition, construction,

	fabrication, remodeling or reconstruction., or otherwise allowable equipment, where (1) the financing is provided by an external third party, (2) the underlying assets support the Federal award, (3) any earnings on debt proceeds invested temporarily are used to offset the current period cost or capitalized interest (amounts subject to arbitrage requirements are exempted), and (4) negotiation may be required in certain circumstances.
Lobbying	Lobbying includes influencing activities associated with obtaining grants, contracts cooperative agreements or loans, and is nonallowable.
Underrecovery of costs under Federal agreements	Any excess costs over the Federal contribution under one award agreement are unallowable under other award agreements.

Attachment C - State/local Wide Central Service Cost Allocation Plans (CSCAP)

General

Such services as motor pools, computer centers, purchasing and accounting are typically provided to operating agencies of a governmental unit on a centralized basis. Federally funded award programs may be included in the operating activities or cost objectives. As such, this attachment establishes a process to identify and assign central services costs to the benefitted activities or objectives on a reasonable and consistent basis. All costs and other data underlying the process should be supported by formal accounting and other records.

Guidelines and illustrations of central service cost allocation plans are provided in a brochure published by the Department of Health and Human Services, entitled *A Guide for State and Local Government Agencies: Cost Principles and Procedures for Establishing Cost Allocation Plans and Indirect Cost Rates for Grants and Contracts with the Federal Government*. This can be obtained from the Superintendent of Documents, U.S. Government Printing Office.

Definitions

Billed central services are those services billed to benefitting agencies, on an individual fee-for-service or similar basis. Typical services included in this category include computer services, transportation services, insurance and fringe benefits.

Allocated central services are services that benefit operating agencies but are not billed on a fee-for-services or similar basis. typically these include general accounting, personnel administration and purchasing.

Agency or **operating agency** means an organizational unit or subdivision within a governmental unit that is responsible for the performance or administration of awards or activities of the governmental unit.

Scope

The CSCAP will include all costs that are to be claimed (billed or allocated) to Federal awards, and must be documented as described below. Costs of central services not included in the CSCAP will not be reimbursed.

Submission requirements

States must submit a plan to the Federal Department of Health and Human Services (DHHS), which must include (1) a projection of next year's central service cost, and (2) a reconciliation of the actual allocated costs to estimated costs for the most recently completed year, or the year immediately preceding the most recently completed year.

"Major local governments" (as designated by OMB) must submit a plan to the cognizant agency annually.

Other local governments must develop a plan in accordance with the requirements of this Circular, and maintain the plan and supporting documentation for audit. They are not required to submit the plan for approval unless specifically requested to do so by the cognizant agency.

All plans will be prepared and (when required) submitted within six months prior to the beginning of each of the governmental unit's fiscal years in which it proposes to claim central services costs. Extensions may be granted by the cognizant federal agency.

Documentation requirements

The attachment states that the requirements for documentation may be altered by the cognizant agency on a case-by-case basis. Alteration may mean modification, expansion or reduction. As an example, a cognizant agency may reduce the requirements for central services where there is little or no impact on Federal awards.

The items below are the guidelines presented in the attachment. Items which are marked with an asterisk (*) should be submitted only once, and in subsequent years, only changes need to be identified.

General All proposed plans must include (1) an organization chart in sufficient detail to show operations including central service activities (whether or not all operations benefit from central services), (2) a copy of the annual financial report (or the executive budget, if budgeted costs are being proposed) to support the allowable costs of each central service activity included in the plan, (3) a certification that the plan was prepared in accordance with the Circular, contains only allowable costs, and treated costs among Federal and nonfederal activities consistently.

Allocated central services For each allocated central service, the plan must include (1) a brief description(*) of the service, (2) an identification of the unit providing the service and the operating agencies receiving the service, (3) the items of expense included in the cost of the service, (4) the method used to distribute the cost of the service to benefitted agencies, and (5) a summary schedule showing the allocation of each service to the specific benefitted agencies. In addition, if any self-insurance funds or fringe benefit costs are treated as allocated (rather than billed) central services, additional documentation is required as discussed below.

Billed services

Internal service funds - For each activity with an operating budget of $5 million or more, the plan shall include (1) a brief description of each service, (2) a balance sheet for each fund based on individual accounts contained in the governmental unit's accounting system, (3) an operating statement, with revenues broken out by source (regular billings, interest earned, etc.), (4) a listing of operating transfers, (5) a description of the methodology used to charge the costs of each service to users (including how billing rates were determined), (6) a schedule of current rates, and (7) a comparison of total revenues generated to the allowable costs of the services, which explains how variances will be handled.

Revenues must be determined on the accrual basis, and must be imputed on users who are not billed. Expenses must be presented by object cost categories (salaries, supplies, etc.).

Self-insurance funds - These funds must include (1) a balance sheet, (2) operating statement, (3) a list of all nonoperating transfers in and out, (4) the types of risk covered by the fund (such as auto liability, worker's compensation, etc.), (5) an explanation of how the level of fund contributions are determined, including actuarial data, with assumptions used, and (6) a description of the procedures used to charge or allocate fund contributions to benefitted activities.

Reserve levels in excess of claims (1) submitted and adjudicated but not paid, (2) submitted but not adjudicated, and (3) incurred but not submitted, must be identified and explained.

Fringe benefits - Fringe benefit plans must present (1) a listing of fringe benefits provided to covered employees, (2) the overall annual cost of each type of benefit, (3) current fringe benefit policies (*) and (4) procedures used to charge or allocate the costs of the benefits to benefitted activities. In addition, for pension and post-employment health insurance plans, the governmental unit must include (1) the government's funding policies, if different from actuarially determined rates, (2)the pension plan's cost accrued for the year, (3) the amount funded and dates of funding, (4) a copy of the current actuarial report (including the assumptions), (5) the plan trustee's report, and (6) a schedule showing the interest cost associated with late funding.

Certificate of Cost Allocation Plan

The central services cost allocation plan shall be accompanied by a certification in the following form:

This is to certify that I have reviewed the cost allocation plan submitted herewith and to the best of my knowledge and belief:

(1) All costs included in this proposal (identify date) to establish cost allocations or billings for (identify period covered) are allowable in accordance with the requirements of OMB Circular A-87, *Cost Principles for State and Local Governments,* and the Federal awards to which they apply. Unallowable costs have been adjusted for in allocating costs as indicated in the cost allocation plan.

(2) All costs included in this proposal are properly allocable to Federal awards on the basis of a beneficial or causal relationship between the expenses incurred and the awards to which they are allocated in accordance with applicable requirements. Further, the same costs that have been treated as indirect costs have not been claimed as direct costs. Similar types of costs have been accounted for consistently.

I declare that the foregoing is true and correct.

Governmental unit ____

Signature____

Name of official ____

Title ____

Date of execution ____

Negotiation and approval of plans

All plans required to be submitted for approval will be reviewed, negotiated and approved by the Cognizant agency on a timely basis (within six months), and must either negotiate or approve the proposal, or advise the governmental unit of any additional information or documentation that will be required in order to do so. Once approved, the plan is to be used by all Federal agencies.

Negotiation results shall be summarized in a written agreement, and only subject to reopening when found to be in violation of applicable law, or where the information upon which the plan is based in determined to be erroneous.

Other policies

Billed central services activities must account for all revenues, expenses and net profit/loss.

Internal service funds are generally allowed to accumulate working capital reserves of up to sixty days. Amounts in excess of that period require approval of the cognizant agency.

Allocated central service costs are generally negotiated and approved for a future year on a "fixed and carry forward" basis.

All plans and related documentation must be retained in accordance with the Common Rule requirements.

Any appeals must be conducted in accordance with the appeals procedures of the applicable cognizant agency.

OMB will lend assistance as required to any problems encountered with the negotiation and approval process.

Attachment D - Public Assistance Cost Allocation Plans

This attachment is not applicable to the program.

Attachment E - State and Local Indirect Cost Rate Proposals

General

Indirect costs are those incurred for common purposes, benefit more than one cost objective and cannot be readily identified with a particular cost objective without efforts disproportionate to the results. Indirect costs are those costs remaining to be allocated after the direct costs have been determined and assigned. Indirect costs may not be assigned to a program if that program has already borne direct costs for the same purpose.

Indirect costs include costs originating in each department or agency of the governmental unit carrying out federal awards and the costs of central governmental services distributed through the central services cost allocation plan, which are not treated as direct costs.

Normally, indirect costs are charged to a program using indirect cost rates. Separate indirect cost rates are generally needed for each department or agency of the governmental unit claiming indirect costs under Federal awards.

The types of indirect costs that may exist cannot be specified in all situations, given the diversity of governmental units. Typical examples of such may include state/local wide central services costs, general administration of the department or agency, accounting and personnel services, depreciation and use allowances, costs of operating and maintaining the facilities, etc.

Definitions

Indirect cost rate proposal means the documentation prepared by a governmental unit to substantiate its request for the establishment of an indirect cost rate.

Indirect cost rate means the device for determining in a reasonable manner the proportion of indirect costs each program should bear. It is the ratio (as a percentage) of indirect costs to a direct cost base.

Indirect cost pool is the accumulation of costs that jointly benefit two or more programs or other cost objectives.

Base means the accumulated direct costs (normally either total direct salaries or total direct costs, excluding any extraordinary or distorting expenditures) used to distribute indirect costs to individual Federal awards. The base selected should provide for a distribution of indirect costs proportional to the benefit received by the activity.

Predetermined rate means the indirect cost rate applicable to a specified current or future period, usually the governmental unit's fiscal year. The rate is based on estimates of costs to be incurred during the period, and is normally not subject to adjustment.

Fixed rate means an indirect cost rate which has the same characteristics as a predetermined rate, except that the difference between the estimated costs and the actual allowable costs is carried forward as an adjustment to the rate computation of a future period.

Provisional rate means a temporary indirect cost rate that is established for funding, interim reimbursement and reporting indirect costs on Federal awards pending the establishment of a final rate.

Final rate means an indirect cost rate applicable to a specified past period which is based on the actual allowable costs of the period. A final rate is not subject to adjustment.

Allocation of indirect cost and determination of indirect cost rates

General Where the governmental unit's department or agency has only one major function, or where all functions that exist benefit to approximately the same degree, the simplified method described below may be used. If several functions exist, or where the benefits are not approximately equal, allocation of indirect costs may require the accumulation of such costs into separate cost groupings which are then allocated on a base which best measures the degree of benefit. The indirect costs are then distributed to individual awards or activities by means of an indirect cost rate.

Simplified method The allocation may be accomplished by (1) classifying the agency's total costs as either direct or indirect, and (2) dividing the total allowable indirect costs (net of credits) by an equitable distribution base. The result is an indirect cost rate which is used to distribute indirect costs to individual Federal awards. The rate should be expressed as a percentage which the total amount of allowable indirect cost bears to the base selected.

Both the direct and indirect costs must exclude capital expenditures and unallowable costs. However, unallowable costs must be included in direct costs, if they represent activities to which indirect costs are properly allocable.

The base may be total direct costs (excluding capital expenditures and other extraordinary items which would distort the allocation process), total direct salaries and wages, or another base which results in an equitable distribution.

Multiple allocation method Separate cost groupings are required when indirect costs benefit the governmental unit's major functions to varying degrees. Each grouping must be allocated on the base that provides the best measure of the relative benefits.

Each grouping should contain items of like character. The number of groupings should be minimized to that which is necessary to provide equitable distribution. When the expenses in a grouping are general in nature, the allocation should be made using a base that is acceptable to both the Federal government and the governmental unit. Generally, any cost element or related factor associated with the governmental unit's activities is adaptable for the base, provided that the factor can readily be expressed in terms of dollars or other quantitative measure. Examples of such factors are total direct costs, total salaries and wages, staff hours applied, square footage, hours of usage, number of documents processed, and population served. Also, the factor must be common to the benefitted functions during the period.

Special indirect cost rates In some cases, a single indirect cost rate for all activities may not be appropriate, as it may not take into account all factors which may affect the indirect costs applicable to a particular program or group of programs. These factors may include physical location of the work, the level of administrative support required, the nature of the facilities, organizational arrangements used or any combination of these factors. In such cases, provision should be made for a separate indirect cost pool applicable to that award.

Federal statutes restrict reimbursement of certain indirect costs. In those cases, it may be necessary to develop a special rate for the award affected.

Submission and documentation of proposals

All departments or agencies desiring to claim indirect costs must prepare and document the indirect cost rate proposal (ICRP). Such documentation and proposal must be retained in accordance with Common Rule requirements.

If a cognizant agency has been assigned, the ICRP must be submitted to the cognizant agency. OMB periodically publishes a list of governmental units which identifies the cognizant agencies for them. For all governmental units not assigned a cognizant agency, the agency that provides the largest amount of Federal assistance is the cognizant agency. These smaller governmental units must prepare and document the ICRP and maintain proposal and related documentation for audit. Only when specifically requested to do so must the smaller governmental units submit an ICRP for approval. If the governmental unit is a subrecipient (it receives no direct assistance), the primary recipient is responsible for negotiating or monitoring the subrecipient's plan.

Indian tribal governments should submit their ICRPs to the Department of Interior.

ICRPs must be developed (and if required, submitted) within six months after the close of the fiscal year, unless the cognizant agency approves a longer period. If the proposed central services cost allocation plan for the same period has not been approved by that time, the ICRP may be prepared including an amount for central services that is based on the latest federally approved central services cost allocation plan. Any adjustment necessary upon approval will be made in a subsequent period.

Each indirect cost rate proposal shall include:

- the rates proposed, including subsidiary worksheets and other relevant data, cross-referenced and reconciled to the financial data below. Allocated central services costs will be supported by the summary table included in the central service cost allocation plan;

- the financial data (financial statements, CAFR, executive budgets, accounting reports) upon which the rate is based. Any adjustments resulting from the use of unaudited data will be adjusted in subsequent periods;

- the approximate amount of direct base costs under Federal awards, broken down between salaries/wages and other direct costs;

- an organizational chart, noting the duties or responsibilities of all units that comprise the agency.

Each ICRP shall contain the certification in the following form:

This is to certify that I have reviewed the indirect cost rate proposal submitted herewith and to the best of my knowledge and belief:

(1) All costs included in this proposal (identify date) to establish billing or final indirect cost rates for (identify period covered by rate) are allowable in accordance with the requirements of the Federal awards to which they apply and OMB Circular A-87, *Cost Principles for State and Local Governments*. Unallowable costs have been adjusted for in allocating costs as indicated in the cost allocation plan.

(2) All costs included in this proposal are properly allocable to Federal awards on the basis of a beneficial or causal relationship between the expenses incurred and the agreements to which they are allocated in accordance with applicable requirements. Further, the same costs that gave been treated as indirect costs have not been claimed as direct costs. Similar types of costs have been accounted for consistently and the Federal Government will be notified of any accounting changes that would affect the predetermined rate.

I declare that the foregoing is true and correct.

Governmental Unit ______________ Signature _________________________

Name of official ________________ **Title** ___________________________

Date of execution ________________

Section V. <u>Audit requirements</u>

<u>When an Audit is Required</u>

Under the provisions of the Single Audit Act of 1996, an audit under OMB Circular A-133 is required whenever the amount of **federal expenditures** (LCDBG program funds plus all other federal expenditures) in a year exceeds $300,000. This type of audit, which includes a full set of financial statements and other detailed information, is often referred to as a "single audit". The single audit will meet federal accountability requirements and will also be sufficient to meet state accountability requirements. If less than $300,000 in total federal funds is expended in an entity's fiscal year, a single audit is not required, but other requirements called for by state law and OCD policy must be met.

If a grantee determines that a single audit is not required, state law and the OCD contract require the submission of one of the following type of reports, based on **revenues received** from all sources during a fiscal year: (1) annual sworn financial statements if revenue received was $50,000 or less, (2) an annual compilation if revenue received was between $50,000 and $350,000, (3) a biennial audit if revenue received was between $350,000 and $3,500,000, or (4) an annual audit if revenue received was in excess of $3,500,000. For each fiscal year that a single audit is not required, the grantee must submit to OCD, no later than six months after fiscal year end, a copy of the appropriate type of report. In addition to the appropriate type of report, the "Total Federal Funds Expenditure Certification" (included in the exhibits section for reference) must also be submitted to OCD which certifies that less than $300,000 of federal funds was expended during the fiscal year.

<u>Audit Scope</u>

When a grantee engages an independent CPA to conduct its audit, a copy of the written engagement agreement must be furnished to the Legislative Auditor of the State of Louisiana for approval of the engagement terms and conditions. The Legislative Auditor will forward to the independent CPA a copy of the approved engagement agreement. Approval is now available via fax or e-mail.

Upon completion of the audit, **in addition to the copies of the audit report filed with the Legislative Auditor, an additional copy, together with all written communications between the audit firm and the grantee, must be furnished to the State of Louisiana, Division of Administration, Office of Community Development.**

Grantee management will be expected to respond in writing to the OCD regarding any findings of noncompliance, control structure comments or recommendations cited by the independent CPA in his or her reports. Such response should identify each finding or comment, state what action has been taken or is planned to be taken, and if action has not yet been taken, the approximate date the action will be completed, or explain why no action is believed to be required.

Audit Costs

If audit costs are to be charged to the LCDBG program, the grantee must follow the "Procurement" guidelines established under the Common Rule. A written procurement policy must be prepared and adopted by the governing body. Such policy should clearly prohibit elected officials, staff, or their agents from obtaining any benefit from procurement contracts.

Specific guidance is presented in the 1997 Handbook at section H. However, due to the importance of the audit process, grantees are reminded that not all CPAs are qualified to perform audits of governmental entities and in particular, under the Single Audit Act. Care should be exercised to select an experienced, qualified firm, rather than simply selecting the firm offering to perform the audit at the lowest price.

The portion of the total audit cost which can be charged to the LCDBG program may be determined by multiplying the total audit cost times a fraction, the numerator of which is the LCDBG program expenditures for the period, and the denominator of which is the government entity's **total** expenditures for the period, including the LCDBG program expenditures. A calculation of the allowable portion of the audit cost should be included in the supporting documentation presented with the request for payment.

Under the latest revisions to OMB Circular A-87, if appropriate documentation of the audit costs provide a higher amount than the formula, the higher audit costs may be charged to the program. Supporting documentation should be available for review by OCD.

Section VI. Monitoring

As a primary recipient, OCD has certain responsibilities to determine that subrecipients (local government grantees) are conducting program activities in accordance with the applicable federal (and state) requirements. (These are the same requirements that apply to the OCD.)

One way in which the OCD discharges its responsibility is by requiring local grantees to furnish OCD with a copy of the single audit or the appropriate type of report required by state law.

Another way of discharging its responsibility is by performing its own monitoring visits to the grantees' offices to review for itself the procedures being followed and make its own assessments about the grantees' performance.

During the monitoring visit, personnel from the OCD will review program records and procedures for compliance with the requirements we have presented in this manual, and the 1997 *Handbook*. At the conclusion of the monitoring, an exit conference will be held to discuss the monitoring team's findings.

The exit conference provides OCD personnel an opportunity to clear up any misunderstandings that may exist, and explain any matters that do not meet OCD requirements. In addition, the exit conference provides the grantee with an opportunity to ask questions about the findings and explore the corrective action needed.

Section VII. Comprehensive case study

The following comprehensive case study illustrates the matters discussed throughout the text. Excerpts from the grant agreement necessary to an understanding of the grant are included. Transactions occurring in the operation of the grant are described, journalized, and posted to the general ledger and subsidiary records, following the modified accrual basis of accounting. Financial statements, including the cumulative budget statement, are generated from the basic records. An attempt has been made to include a variety of transactions in the case study, addressing most, if not all, situations that may arise in administering the program. Should any questions arise, grantees are requested to examine the sample transactions for a possible solution prior to contacting the OCD for technical assistance.

The following transactions and events relate to Sample Town, a small municipality who was awarded a small LCDBG grant to make improvements to the water treatment facility. The grant budget is presented below. Sample Town's fiscal year ends on December 31 of each year.

Budgeted Revenues:	
LCDBG grant	$ 550,000
FmHA grant	75,000
General fund	35,000
Total	$ 660,000
Budgeted Expenditures:	
Administrative	$ 35,000
Acquisition	33,000
Engineering	42,000
Construction	550,000
Total	$ 660,000

Transactions

Date	Transaction description
May 15	Sample Town receives an invoice from Joe Consultant & Associates in the amount of $3,500.
May 28	Sample Town issues general fund check #65170 to Joe Consultant & Associates for $3,500.
May 29	Sample Town receives invoice #1 from Ace Construction Company for $315,000 ($350,000 less 10% retainage).
May 30	Sample Town submits Request for Payment #1 for $315,000.
June 10	$315,000 is deposited into Sample Town's LCDBG checking account.
June 11	Sample Town issues Check #101 to Ace Construction Company for $315,000.
June 13	Sample Town receives invoice #1 from Project Engineering in the amount of $30,000.
June 17	Sample receives an invoice from Tom Taxpayer for right of way acquisition for $33,000.
June 20	Sample Town submits request for reimbursement to FmHA for $63,000.
July 2	$63,000 is deposited into Sample Town's LCDBG checking account.
July 3	Sample Town issues checks #102 to Project Engineering for $30,000 and #103 to Tom Taxpayer for $33,000.
Aug 10	Sample Town receives invoice #2 from Ace Construction Company for $180,000 ($200,000 less 10% retainage).
Aug 10	Sample Town receives invoice #2 from Project Engineering for $8,000.
Aug 10	Sample Town receives an invoice from Joe Consultant & Associates for $31,100.
Aug 11	Sample Town submits Request for Payment #2 for $180,000, and requests $8,000

from FmHA.

Aug 18	Sample Town issues general fund check #66144 to Joe Consultant & Associates for $31,100.
Aug 20	$188,000 is deposited into Sample Town's LCDBG checking account ($180,000 from LCDBG and $8,000 FmHA).
Aug 21	Sample Town issues check #104 to Ace Construction Company for $180,000 and check #105 to Project Engineering for $8,000.
Aug 28	The project is inspected and determined to be substantially completed.
Sept 10	Sample Town receives invoice #3 (final) from Ace Construction Company for the retainage amount of $55,000, and invoice #3 from Professional Engineering for $4,000.
Sept 11	Mildred Justrite, Sample Town Clerk, prepares and submits a properly approved time sheet for services performed on the LCDBG program in the amount of $400.
Sept 12	Sample Town submits Request for Payment #3 in the amount of $55,000, and requests $4,000 from FmHA.
Sept 19	$59,000 is deposited into Sample Town's LCDBG checking account.
Sept 20	Sample Town issues checks #106 to Ace Construction Company for $55,000 and #107 to Project Engineering for $4,000.
Sept 30	Since the project is now complete, financial statements are prepared to reflect the activity of the grants.

Appendix

Contact list

Name	E-mail address
William Hall	whall@doa.state.la.us
Henry Sheffield	hsheffi@doa.state.la.us
Sandy Smith	ssmith2@doa.state.la.us
L. Wayne Dale	ldale@doa.state.la.us

State of Louisiana
Division of Administration
Office of Community Development
State Capitol Annex, Room 168
Post Office Box 94095
Baton Rouge, Louisiana 70804-9095

Telephone	(504) 342-7412
Fax	(504) 342-1057
TDD	(504) 342-7422
LINC	421-7412

Other web addresses of importance:

Louisiana Legislative Auditor
www.lla.state.la.us

Office of Management and Budget
www.whitehouse.gov/OMB

OMB Compliance Supplement
www.whitehouse.gov/OMB/Grants/A133_Compliance/

Catalog of Federal Domestic Assistance
www.gsa.gov/fdac/

EXHIBITS